TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1939

No. 426

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

STEPHEN J. LEONARD

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR CERTIORARI FILED SEPTEMBER 29, 1939

CERTIORARI GRANTED FEBRUARY 5, 1940

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1 Before United States Board of Tax Appeals

Docket No. 65805

STEPHEN J. LEONARD, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Docket entries

Appearances: For Petitioner, J. Donald Duncan, Esq., Dean Acheson, Esq., P. M. Wormhoudt, Esq. For Respondent, Frank M. Thompson, Esq., Dean P. Kimball, Esq.

1932

May 7—Petition received and filed. Taxpayer notified. (Fee paid.)
May 7—Copy of petition served on General Counsel.
June 8—Answer filed by General Counsel.
Aug. 18—Copy of answer served on taxpayer—General Calendar.

1936

Oct. 5—Hearing set Dec. 2, 1936.
Oct. 8—Motion for circuit hearing at New York City filed by taxpayer. 10/10/36, granted.
Dec. 12—Hearing set week of Nov. 30, 1936, in New York City.
2 Dec. 2—Hearing had before J. M. Sternhagen, Division 10. On motion of respondent to dismiss for failure of petitioner to appeal and prosecute. Motion granted and petition dismissed.
Dec. 8—Order of dismissal entered—J. M. Sternhagen, Division 10.
Dec. 22—Notice of appearance of Dean Acheson as counsel filed.
Dec. 22—Notice of appearance of M. P. Wormhoudt as counsel filed.
Dec. 23—Motion to vacate order of dismissal and to place on the New York City Circuit Calendar filed by taxpayer. 12/23/36, granted.
Dec. 23—Order vacating order of dismissal and restoring proceeding to the New York City Circuit Calendar entered.
Dec. 31—Transcript of hearing of 12/2/36, filed.

1937

Jan. 29—Hearing set week of 2/15/37 at New York, N. Y.
Feb. 6—Application for subpoena filed by taxpayer.
Feb. 8—Subpoena duces tecum to Lloyd A. Waugh issued.
Feb. 8—Subpoena duces tecum to C. O. Sayward issued.

1937

Feb. 15—Hearing had before Mr. Arnold, Division 12, on the merits. Submitted. Petitioner's brief due March 31, 1937—respondent's brief due 4/30/37—petitioner's reply brief due 5/15/37.

3 Feb. 26—Transcript of hearing Feb. 15, 1937, filed.

Mar. 26—Brief filed by taxpayer. 3/26/37 copy served on General Counsel.

Apr. 29—Brief filed by General Counsel.

May 15—Reply brief filed by taxpayer.

Sept. 28—Findings of fact and opinion rendered—Wm. W. Arnold, Division 12. Decision will be entered under Rule 50.

Oct. 26—Notice of settlement filed by General Counsel.

Oct. 28—Hearing set Nov. 17, 1937, on settlement.

Nov. 5—Motion to substitute the attached recomputation in place of that filed Oct. 26, 1937, filed by General Counsel. 11/8/37 copy served.

Nov. 13—Consent to settlement filed by taxpayer.

Nov. 23—Decision entered—Wm. W. Arnold, Division 12.

1938

Feb. 9—Petition for review by U. S. Circuit Court of Appeals, Second Circuit, with assignments of error filed by General Counsel.

Feb. 14—Petition for review by U. S. Circuit Court of Appeals, Second Circuit, with assignments of error filed by taxpayer.

Feb. 14—Proof of service filed by taxpayer.

Feb. 16—Proof of service filed by General Counsel (taxpayer).

Feb. 19—Proof of service filed by General Counsel (counsel).

Mar. 30—Stipulation for consolidated record of petitioner and respondent, for division of cost of printing, and provision for filing briefs—subject to approval by the Circuit Court of Appeals—filed.

4

1938

Mar. 30—Joint statement of evidence lodged by the parties.

Mar. 30—Joint praecipe for record filed by the parties.

Mar. 31—Joint statement of evidence approved and ordered filed.

Apr. 7—Order enlarging time for transmission and delivery of record to May 23, 1938, entered.

Before United States Board of Tax Appeals

[Title omitted.]

Petition

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency IT: AR: A-1 GC-60D (dated March 11, 1932), and as a basis of his proceedings, alleges as follows:

5 1. The petitioner is an individual with a residence at 1067 Fifth Avenue, New York, N. Y.

2. The notice of deficiency (a copy of which is attached and marked Exhibit A) was mailed to the petitioner under date of March 11, 1932.

3. The taxes in controversy are income taxes amounting to $3,270.27.

4. The determination of tax set forth in said deficiency notice was based upon the following errors:

(a) The notice of deficiency states that there will be added to the income reported by the petitioner for the calendar year 1929 the income reported by the United States Trust Company of New York in the sum of $17,723.89 plus income distributed by said trustee to Mrs. Adelaide Leonard and children amounting to $16,191.34, thus increasing the net income of the petitioner for that year from $22,411.89 to $56,327.12.

(b) The notice of deficiency states that from the aforesaid trust instrument it would appear that the provisions made for the payment of income to Mrs. Adelaide Leonard and her children were for their support or in lieu of an allowance which in the event of the granting of a divorce the court would have made and that following the case of Mary R. Spencer et al. published in 20 Board of Tax Appeals 58 it is proposed in the notice of deficiency that the income from the aforesaid trust fund should be taxable to the petitioner.

6 5. The facts upon which the petitioner relies as the basis of this proceeding are as follows:

(a) That on or about the 27th day of December 1928, petitioner was served with a summons in the Supreme Court of Ulster County of the State of New York in an action for absolute divorce instituted by his then wife, Adelaide S. Leonard; that the petitioner appeared by counsel in said proceeding and that subsequent to said appearance and prior to the actual trial of said action petitioner's said counsel and counsel for Mrs. Adelaide S. Leonard negotiated over an extended period of time the question of the

property rights of the petitioner and his said wife, the said wife being possessed at that time of considerable property which the petitioner had given her during the time of their married life.

(b) That at the time of the institution of an action by Mrs. Adelaide S. Leonard (hereinafter referred to as the "wife") for a divorce from the petitioner the petitioner was a man of wealth actively engaged in business and possessed of a substantial income; that in addition petitioner had given to the said wife during the course of their married life of approximately twenty years a considerable amount of property which was at the time of the institution of said action worth many thousands of dollars in real and personal property.

7 (c) That after the institution of the aforesaid action for divorce counsel for the wife and the petitioner discussed the question whether and to what extent the wife would be entitled to alimony, and upon information and belief said counsel were in agreement that under the laws of the State of New York a wife, if successful in an action for a divorce from her husband, though possibly entitled to the payment of some sum of money per year for alimony and support of dependent children in an amount based upon the income of the husband, the husband could not be forced to pay to the wife any amount of property except from income.

(d) That after many extended conferences of counsel for the wife and the petitioner two agreements were executed between the wife and the petitioner, both dated June 4, 1929; one entitled "Separation Agreement between Adelaide Shanahan Leonard and Stephen J. Leonard" and the other entitled "Agreement between Stephen J. Leonard, United States Trust Company of New York, and Adelaide Shanahan Leonard."

(e) That by the terms of the aforesaid Separation Agreement dated June 4, 1929, between the wife and the petitioner recitation was made of the fact that the petitioner by separate agreement under even date therewith had established a trust fund with a principal of $650,000, the net income of which was to be

8 payable to the wife subject to a prior charge of $15,000 in favor of the three children of the wife and the petitioner; said Separation Agreement then further stated that in addition to the establishment of the aforesaid trust fund the wife had received in the past by way of gifts from the petitioner personal property then having a value of $350,000 with a then income value of at least $15,000 so that the wife agreed that as of the date of the execution of the Separation Agreement she had an income of at least $30,000 from the aggregate net income of the property given to her by her husband and from the aforesaid trust fund, subject only to the necessity to pay for

the support, maintenance, and education of the aforesaid three children; the aforesaid Separation Agreement of June 4, 1929, further provided that the petitioner would pay to the wife for the support and maintenance of the wife and the said three children

"(1) On the 15th day of June in each year, beginning with the year 1929, the sum of $10,000, and

"(2) In addition the sum of $25,000 per year, to be paid so far as arithmetically possible in equal monthly payments on the first day of each month beginning with the month of July 1929."

Said payments of $35,000 per year to be paid during the life of the wife provided the petitioner's circumstances and ability to pay the same continued to be as good or better than as of
9 the date of the execution of the said agreement. In addition to the aforesaid $35,000 per year the petitioner agreed to pay any extraordinary medical or surgical expenses incurred by the wife or on behalf of the aforesaid three children until the time when each child respectively attained the age of twenty-five years.

(f) That the trust agreement dated June 4, 1929, between the petitioner, United States Trust Company of New York, and the wife, which is referred to in the notice of deficiency, was a fund established by the petitioner with a principal of approximately $650,000; the net income therefrom was payable to the extent of $5,000 per year each to the three children of the petitioner (except that during their minority the same should be paid to the mother for their account and if any said child should die during the life of the wife the amount then payable to the child should be payable to the wife), and the entire balance of the net income over $15,000 in the aggregate, which, as aforesaid, was payable to the children, is by the terms of said trust agreement payable to the wife, and upon her death the principal of said trust fund is divisible into as many equal parts as there shall be then living children of the wife and the petitioner and deceased children of the wife and the petitioner leaving issue, and said principal is paid over then to said children and said issue with minor provisions that the same may be held during minority and paid at majority.

10 (g) That the petitioner established said trust fund with the United States Trust Company for the protection of his said children and that therefore if the said children were not to be placed in the sole custody of his wife there was no reason for the establishment of said trust fund.

(h) That in order to protect his legal rights petitioner insisted that said trust fund should not become irrevocable unless the wife

secured an absolute divorce and the custody of the children but that if she did receive such divorce and the custody of said children pursuant to a valid decree of a court of competent jurisdiction, then in such event the trust fund should become irrevocable and title to the trust res pass to the trustee for the benefit of the children of the petitioner and their issue, subject only to the payment of part of the income therefrom to the wife during her life.

(i) That the action instituted by the wife for a divorce from the petitioner was duly prosecuted in court and under date of July 10, 1929, the referee rendered his report in favor of the said wife and under date of July 19, 1929, a decree by the Honorable William [illegible] Collins, Justice of the Supreme Court of New York State, ordered, adjudged and decreed that the wife was entitled to a judgment that the marriage between the wife and the petitioner be dissolved and that the agreement of June 4, 1929 (being
11 the Separation Agreement) providing for the custody of the minor children of said marriage and providing for the support and maintenance of the wife was approved and that the wife have the custody of said children and that the defendant (the petitioner herein) pay to the wife during the term of her natural life the sum of $35,000 per year; that said order of said court is still in full force and effect and carries out the terms of said Separation Agreement.

(j) That the final decree of divorce was served upon the Trustee, United States Trust Company, and the second of said agreements of June 4, 1929, being the aforesaid trust agreement, thereupon became irrevocable and petitioner from and after said date had no interest whatsoever in either the income or the principal of said property, the said property being the property of his children, subject, as aforesaid, to the rights of the wife in part of the income thereof.

(k) That the aforesaid facts are not the same as the facts set forth in the case of Mary R. Spencer et al., published in 20 Board of Tax Appeals 58, in that in said case the husband received income and was entitled to receive income from the trust fund established by the husband, only part of said income being payable to the wife, and said trust fund was established in lieu of alimony.

(l) That in petitioner's case the trust fund established was in connection with the property rights of the children, the wife and the petitioner as a basis of settlement, and from
12 said agreement, which will be produced upon the trial of this petitioner, if tried, it will be observed that the wife placed in the trust fund certain insurance policies aggregating some $300,000 upon the life of the petitioner, in which policies the wife

was named as beneficiary, and said agreement of trust is a settlement of property rights which have been determined and which from and after the date of the final decree of divorce definitely established the property in the trust fund as entirely separate from any interest whatsoever of the petitioner who was entitled to no income therefrom and therefore cannot be taxed thereon.

(m) That payments under said trust fund are not in lieu of alimony as the petitioner was required to pay alimony of $35,000 per year entirely separate and apart from said trust agreement.

Wherefore your petitioner prays that this Board may hear the proceeding and grant relief to the petitioner so that the Board will find that the petitioner is entitled to have the proposed deficiency of $3,270.27 for the calendar year 1929 cancelled and that there is no deficiency due from the petitioner.

Dated New York, N. Y., May 4, 1932.

(Sgd.) J. DONALD DUNCAN,
J. Donald Duncan,
Counsel for Petitioner,
50 Broadway, Borough of Manhattan,
City and State of New York.

13 [*Duly sworn to by Stephen J. Leonard; jurat omitted in printing.*]

14 *Exhibit A annexed to foregoing petition*

[Copy]

TREASURY DEPARTMENT,
Washington, Mar. 11, 1932.

Mr. STEPHEN J. LEONARD,
465 Park Avenue, New York, New York.

SIR: You are advised that the determination of your tax liability for the year(s) 1929 discloses a deficiency of $3,270.27, as shown in the statement attached.

In accordance with Section 272 of the Revenue Act of 1928, notice is hereby given of the deficiency mentioned. Within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter, you may petition the United States Board of Tax Appeals for a redetermination of your tax liability.

However, if you do not desire to petition, you are requested to execute the enclosed agreement form and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C:P-7. The signing of this agreement will expedite the closing of your return(s) by permitting an early assessment of any deficiency and preventing the accumulation of interest charges, since the interest period terminates thirty days

after filing the enclosed agreement, or on the date assessment is made, whichever is earlier; whereas if no agreement is
15 filed, interest will accumulate to the date of assessment of the deficiency.

Respectfully,

DAVID BURNET,
Commissioner.

By J. C. WILMER,
Deputy Commissioner.

Enclosures:
Statement.
Form 882.
Form 870.

[Copy]

STATEMENT

IT: AR: A-1.
GC-60D.

In re: Mr. Stephen J. Leonard, 465 Park Avenue, New York, New York

TAX LIABILITY

Year, 1929; tax liability, $3,613.10; tax assessed, $342.83; deficiency, $3,270.27.

Reference is made to your 1929 income tax return and to the return filed by the United States Trust Company of New York, as trustee, for a trust created by you for the benefit of your wife and children.

16 You are advised that it is held by this office that the income of the trust is properly taxable to you instead of to the beneficaries named in the trust instrument.

Article 7 (a) of the trust deed reads in part as follows:

"Until the time mentioned in sub-paragraph (b-1) of subdivision (b) of this Article, the Grantor hereby expressly reserves the right to amend this instrument and the trust hereby created in any respect whatsoever and as often as desired and also to revoke the same either in whole or in part by an instrument signed by the Grantor and delivered to the Trustee. * * *

"(b) If at any time the third party shall during her life institute any legal proceeding or action for divorce or for the annulment of her marriage with the Grantor, the following provisions shall become effective.

"(b–1) Immediately upon the delivery to the United States Trust Company of New York, the corporate trustee hereunder, of a copy of a Summons and Complaint (with an affidavit of service upon the Grantor and annexed thereto) in an action for divorce or annulment of the marriage of the Grantor and the third party, the right of the Grantor to amend or revoke this instrument as permitted by Article 7 hereof shall be suspended forthwith until such time as there shall be delivered to the said United States Trust Company of New York either (i) a
17 certified copy of a final decree of divorce or annulment of marriage of the Grantor and the third party, or (ii) a copy of a Stipulation executed by the attorneys for the Grantor and the third party evidencing the fact that the aforesaid action for divorce for annulment of the marriage of the Grantor and the third party has been discontinued, or (iii) a certified copy of an order dismissing the aforesaid action. If during said period of suspension there shall be delivered to United States Trust Company of New York, the corporate Trustee hereunder, a certified copy of a final decree of divorce or annulment of the marriage of the Grantor and the third party, the right of the grantor to amend or revoke this instrument as permitted by Article 7 hereof shall terminate ipso facto and this instrument shall thereafter be construed, so far as the Grantor is concerned, as an irrevocable Trust Agreement, and the said United States Trust Company of New York shall have no further liability to the Grantor for any reason whatsoever, * * *"

The information in the file fails to disclose whether a divorce was granted during the year 1929. However, from the trust instrument it would appear that the provisions made for the payment of income to your wife for your children was for their support or in lieu of an allowance which, in the event of the granting of a divorce, the Court would have made. In this connection see appeal of Mary R. Spencer et al., published in 2 Board of Tax Appeals 58.

18 In the above-named case it was held that payments made from a trust fund for the maintenance of a wife and child were in the nature of alimony and not taxable to the recipient. The obligation to make such payments was the obligation of the husband and the payments so made to the wife were made in satisfaction or payment of the husband's personal obligation in that respect.

It is accordingly held that the income from the trust set up for the benefit of your wife and children is properly taxable in your return.

Your return has been adjusted as follows:

Net income reported		$22,411.89
Plus:		
Income reported by trustee		17,723.89
Income distributed by trustee to Mrs. Leonard and children		16,191.31
Adjusted net income		$56,327.12

COMPUTATION OF TAX

Adjusted net income		$56,327.12
Less:		
Exemption	$4,700.00	
Dividends	82,408.25	
		87,108.25
Balance subject to normal tax		None
Surtax on $56,327.12		$3,849.07
Less: Tax paid at source		235.97
Total tax assessable		$3,613.10
Tax previously assessed		342.83
Deficiency		$3,270.27

Due to the fact that the statute of limitations will presently bar any assessment of additional tax against you for the year 1929, the Income Tax Unit will be unable to afford you an opportunity to discuss your case before mailing formal notice of its determination as provided by Section 274 (a) of the Revenue Act of 1926 and/or Section 272 (a) of the Revenue Act of 1928. It is, therefore, necessary at this time to issue this formal notice of deficiency.

A copy of this letter has been mailed to your representative, Mr. B. H. Faulkner, 29 Warfield Street, Upper Montclair, New Jersey, in accordance with the authority conferred upon him in the power of attorney executed by you and on file with the Bureau.

Before United States Board of Tax Appeals

[Title omitted.]

Answer

The Commissioner of Internal Revenue by his attorney, General Counsel, Bureau of Internal Revenue, for answer to the petition of the above-named taxpayer admits and denies as follows:

1. Admits all the material allegations in paragraph 1 of the petition.

2. Admits all the material allegations in paragraph 2 of the petition.

3. Admits that the taxes in controversy are income taxes.

4 (a) and (b). Denies that respondent erred in the determination of the deficiency as alleged in subparagraphs (a) and (b) of paragraph 4 of the petition.

5 (a) to (m). Denies all material allegations contained in subparagraphs (a) to (m), inclusive, of paragraph 5 of the petition.

21 6. Denies generally and specifically each and every material allegation contained in the petition of the above-named taxpayer not hereinbefore expressly admitted, qualified, or denied.

Wherefore, it is prayed that the petitioner's appeal be denied.

(Signed) C. M. CHAREST,
General Counsel,
Bureau of Internal Revenue.

Of Counsel:

FRANK A. SURINE,
Special Attorney,
Bureau of Internal Revenue.

Before United States Board of Tax Appeals

STEPHEN J. LEONARD, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Docket No. 65805. Promulgated September 28, 1937

Findings of fact and opinion

On June 4, 1929, by separate instruments, one a separation agreement and the other a declaration of trust incorporated in the separation agreement by reference, petitioner provided for the maintenance and support of his estranged wife, and for the maintenance, support, and custody of his children. He re-
22 tained no reversionary interest in the trust corpus or income upon termination of the trust. Prior thereto his wife had instituted proceedings for absolute divorce. On October 22, 1929, she received a final decree, which incorporated the provisions of the separation agreement and trust as a part of the court's judgment. Petitioner could revoke the trust if his wife did not prosecute her suit to final decree of divorce and thereafter he could alter or amend the trust agreement with his

wife's consent and no vesting of any interest in his children was permitted under the trust that would prevent a change by him with his wife's consent. During the taxable year the trustee made distributions to the wife and children of trust income. Held, income of the trust distributed in the taxable year, except that portion thereof paid to his adult child, is taxable to grantor, since such income was used to partially discharge his legal obligation to support and maintain his wife and minor children.

J. Donald Duncan, Esq., for the petitioner.

Dean P. Kimball, Esq., for the respondent.

This case involves an alleged income tax liability of petitioner for the year 1929 in the amount of $3,270.27. The deficiency arises from the proposed adition to the petitioner's taxable income for the year 1929 of:

23 (a) The sum of $17,723.89 reported by the United States Trust Co. of New York as capital gains and profits to a trust fund from the sale of bonds held as part of the trust corpus which was not distributable to the beneficiaries.

(b) The sum of $16,191.34 income of the aforesaid trust fund, consisting of dividends and interest received by the trustee and distributable to Adelaide Shanahan Leonard (the former wife of the petitioner) and the three children of the petitioner. Both of these sums were reported for income tax purposes by the United States Trust Co. of New York as trustee in the taxable year.

Respondent confessed error in including in petitioner's taxable income the capital gain reported by the trustee from the sale of capital assets of the trust. Therefore, the only question presented is the taxability of the $16,191.34.

Findings of Fact

At the date of execution of the instruments hereinafter mentioned the petitioner, an individual residing in New York City, was worth approximately $2,000,000. He and his wife, Adelaide Shanahan Leonard, were then living separate and apart. Three children had been born of their marriage, two of whom, Stephanie and Craigh, were minors during the taxable year, and one of whom, Jeanne, became 21 years of age July 18, 1929.

24 Prior to the taxable year and on December 27, 1928, petitioner had been served with a summons in an action for absolute divorce instituted by his wife, Adelaide Shanahan Leonard.

Thereafter, and on June 4, 1929, the petitioner, his wife, and the United States Trust Co. of New York executed an agreement of trust wherein the United States Trust Co. was made trustee, and the petitioner, as grantor, contributed securities, stock, and

cash of the then value of $650,000, listed as Exhibit A, to the trust agreement, as a trust fund, the net income therefrom to be paid to the beneficiaries therein named in equal monthly installments as far as practicable. The trust fund contained $400,000 principal amount of McCullough Oil Co. bonds which petitioner guaranteed as to principal and interest, and in case of default he agreed to substitute cash or securities in lieu thereof.

The grantor reserved the right to amend or revoke the trust instrument until delivery to the trustee of a copy of summons and complaint in a proceeding for divorce by the wife against the husband, and upon such delivery the right to amend or revoke was to be suspended until a certified copy of a final decree of divorce was delivered to the trustee, or a stipulation of attorneys that the divorce action had been discontinued or dismissed was delivered to the trustee. Upon delivery of a certified copy of final decree of divorce to the trustee, grantor's right to amend or revoke was to terminate and thereafter the trust was to be considered irrevocable so far as grantor was concerned.
25 Upon discontinuance or dismissal of the divorce action, the right of revocation was to be in effect and the trust considered a revocable trust. Upon revocation the trust fund and accumulated income was to be fully restored to grantor.

From the net income of the trust during the life of the wife, $5,000 per year was to be paid by the trustee to each of the three named children, the minors' portion payable to the wife as natural guardian for the account of the minors during their minority. Should any child die during the life of the wife, such child's portion was payable to the wife during her life for her own separate use, the remaining net income of the trust to be paid to the wife "during her life to be used by her for her maintenance and support and in her sole discretion for the support, maintenance and education of the children by herself and grantor."

Upon the death of the wife the trust fund was to be divided into as many equal parts as there were then living children and deceased children of the wife by the grantor leaving issue. Each part was to constitute a separate trust fund for the benefit of each living child as life beneficiary and during the minority of each child, so much of the net income as the trustee deemed proper was to be used for the support, maintenance, and education of such minors. The unexpended net income was to be accumulated for such child's benefit upon reaching majority. Upon a child's attaining 21 years, the accumulations and the whole of the net income of such child's portion was to be paid that child in monthly
26 payments during life, and upon the death of such beneficiary, whether before or after attaining 21 years, the principal, together with the accumulations thereon, was to be paid as

such life beneficiary may have directed by will, or in default of such direction, to his or her issue surviving, and if no issue survived, then to the other descendants then living of the wife by the grantor, per stirpes, or if none, to the descendants of the grantor per stirpes.

Should any child die before the wife, having directed by will to whom the payment of his or her portion should be made, payment was to be made in accordance with such direction. In default of any such direction, payment was to be made to his or her issue then living, and if none were living at the time of the wife's death, then to the other descendants of the wife by the grantor, and, if no such other descendants, then to the descendants of grantor.

It was further provided that, notwithstanding any of the terms or provisions rendering the trust irrevocable after a certificate of final decree of divorce was delivered to the trustee, the trust agreement or any of its terms could be changed or amended during the life of the grantor with the consent of the wife and that nothing in the trust agreement should be decreed to vest any interest in the children prior to the death of the grantor or his wife and that no child should have the right to object to any change that might be made by the grantor with his wife's consent.

On the same day, June 4, 1929, a separation agreement was entered into, in which it is recited among other things:

27 "Whereas the parties hereto desire to enter into an agreement by the terms of which they may hereafter continue to live separate and apart and by the terms of which proper and reasonable provision shall be made for the maintenance and support of the party of the first part [wife] and the maintenance, support and custody of the aforesaid two daughters and son, and

"Whereas, by separate trust agreement bearing even date herewith by and between second party as grantor and United States Trust Co of New York, of 25 Wall Street, Borough of Manhattan, City and State of New York, as trustee, some provision has been made by the second party for the maintenance and support of the first party and the aforesaid two daughters and son, which trust agreement is incorporated herein by reference thereto as though fully and at length set forth and is marked Exhibit A."

Summarized, so far as material here, the separation agreement states that the second party (husband) has by the trust agreement established a trust fund with principal amount of $400,000 McCullough Oil Co. 3-year 6-percent first-mortgage sinking fund gold bonds of March 1, 1929, and $250,000 cash or other securities, the net income of which trust is payable to the first party (wife) subject to a prior charge of $15,000 in favor of the three children of the parties. That in addition to the establishment

of the trust fund the wife received in the past by way of
28 gifts from the husband, personal property then of the value of $350,000 which was acknowledged to have a present income value of at least $15,000 and the wife agreed that her income would be at least $30,000 a year from the aggregate net income of the property given her by her husband and from the trust fund, subject only to the necessity of providing therefrom for her support and the support, maintenance, and education of the three children.

The petitioner further agreed to pay his wife the sum of $35,000 per year, $10,000 payable on the 15th day of June in each year, begining with the year 1929, and $25,000 payable in equal monthly payments so far as arithmetically possible on the first of each month, beginning with the month of July 1929. Such payments in the aggregate sum of $35,000 were to be made by the husband to the wife during her life, provided his circumstances and ability to pay continued to be as good or better than of that date, making the aggregate net income receivable by the wife to be used by her for her maintenance and support and that of the three children approximately $65,000 per year from property represented by gifts received from the husband, the trust fund, and the yearly payment under the separation agreement. He further agreed to pay all the extraordinary medical expenses of the wife and children until each child reached the age of 25 years. Either party had the right to apply to the court for readjustment of the $35,000 annual payment as ability to pay varied, but in no case to exceed that amount.

29 In addition to the $650,000 property and cash contributed to the trust fund by grantor, the wife deposited three insurance policies, each of $100,000, in the trust fund, on the life of the husband in which she was the beneficiary. Premiums were to be paid by the wife, and in case of default, grantor could pay them and deduct the amount so paid from the payments due her. The furniture and personal property in a dwelling on Long Island and the city apartment then occupied by the wife were to be her property, including the automobiles, and she was to have the sole care, custody, and control of the children.

Paragraph 8 of the separation agreement provided as follows: "Eighth: The first party hereby accepts the establishment of the Trust Fund (Exhibit A) and the payments to be made by the second party pursuant to this Agreement in lieu of all dower, and hereby releases the second party and his estate from any claim of dower in the property of the second party as now or hereafter constituted."

The insurance policies were surrendered in 1931 and the cash surrender value of $54,640 was paid into the trust fund and became part of the principal of the trust pursuant to the agreement of the parties.

Three changes or amendments were made to the trust agreement in accordance therewith with the wife's consent, none of which are material so far as the issues here involved are concerned.

30 Subsequent to the execution of the trust agreement and the separation agreement, and on July 22, 1929, petitioner's wife obtained an interlocutory decree of divorce from the petitioner. This decree became final October 22, 1929, and a copy of the final decree of divorce was served on the United States Trust Co., October 23, 1929. The court incorporated the agreements in the decree as follows:

"Ordered, adjudged, and decreed that the agreement, Exhibit 3, dated June 4, 1929, providing for the custody of the minor children, Craig Leonard and Stephanie Leonard, issue of said marriage, as well as providing for the support and maintenance of the plaintiff, be and hereby is approved and affirmed and made a part of the judgment herein, and as provided in said agreement, Exhibit 3, dated June 4, 1929, it is

"Ordered, adjudged, and decreed that the plaintiff herein, Adelaide S. Leonard, have the sole care, custody, and control of the infant children Craig Leonard and Stephanie Leonard and that the defendant herein, Stephan J. Leonard pay to the plaintiff herein, Adelaide S. Leonard, for and during the term of her natural life the sum of thirty-five thousand dollars ($35,000) per year; * * *"

During the period June 4 to December 31, 1929, the United States Trust Co. under the trust agreement received income in the sum of $16,191.34 as dividends and interest, and $17,723.89

31 as capital gain from the sale of the oil company bonds in the trust corpus.

Of the distributable income the trustee from June 4 to the end of the calendar year 1929 distributed $5,200 to the wife, $2,083.33 to petitioner's adult daughter, Jeanne Leonard, directly, and to Stephanie and Craigh, minors, each $2,083.33 the minors' portion being paid to their mother as guardian for their account. This left a balance on hand at the close of the calendar year which was not distributed.

Opinion

ARNOLD: The question for our determination is whether all or any part of the $16,191.34 received as income by the trustee from June 4 to December 31, 1929, is taxable to petitioner. The Commissioner included it all in his assessment of deficiency and petitioner claims no part of it is taxable to him.

At the time the separation agreement and the trust agreement were executed: June 4, 1929, petitioner and Adelaide Leonard were husband and wife. An action for divorce was pending by the wife against petitioner. The marriage relationship imposed on petitioner a legal obligation to support and maintain his wife. As a father he was under legal obligation to support and maintain his children during their minority.

The court has authority in dissolving the marriage relationship to make provision for the future support and maintenance of the wife and minor children. In arriving at a suitable amount
32 for this purpose the court takes into consideration the wealth and standing of the parties, their habits of living and surrounding circumstances, and what the parties themselves consider a suitable allowance in view of their agreements.

Pending the divorce proceedings negotiations were conducted between the husband and the wife for the adjustment of this legal obligation. These negotiations culminated in the execution of the separation agreement and the trust agreement of June 4, 1929. Thereafter and on July 22, 1929, petitioner's wife obtained an interlocutory decree of divorce, which became final October 22, 1929.

The petitioner was a wealthy individual with an estate valued at about two million dollars. His family consisted of his wife and three children, two of whom were minors.

The separation agreement recited that some provision had been made in the trust agreement for the maintenance and support of the wife and children and the trust agreement was incorporated therein as though fully and at length set forth.

By the trust agreement petitioner put up cash and securities in the amount of $650,000, from the net income of which $5,000 per year was payable to each of the three children of the wife and petitioner, and the remaining net income to the wife "during her life to be used by her for her maintenance and support, and in her sole discretion for the support, maintenance, and education of the children by herself and the grantor," the portion of income of any child that might die during the lifetime of the wife likewise to be paid the wife.

We think the purpose of both instruments was to make
33 suitable provision for the support and maintenance of the wife and minor children, that they should be construed to that end, and that insofar as provision was made in the trust agreement for the future support of the wife and minor children it was in fulfillment of the legal obligation the marriage relation imposed on petitioner and the natural obligation a father has to support his minor children.

The court had both the separation agreement and the trust agreement before it when it entered its order in the divorce proceeding. When the court by its order and decree approved and affirmed the separation agreement and made it a part of its judgment, in accordance with its provisions, the trust agreement likewise became a part of the decree and was approved and affirmed, as the separation agreement referred to the trust agreement in the following language:

"* * * some provision has been made by the second party [petitioner] for the maintenance and support of the first party [wife] and the aforesaid two daughters and son, which trust agreement is incorporated herein by reference thereto as though fully and at length set forth, and is marked Exhibit A."

Considering the extent of petitioner's estate, it is reasonable to suppose that, but for the benefits accruing to the wife and minor children from the trust income, she would have asked for and the court would have awarded an amount in excess of that provided in the separation agreement for her support and maintenance and that of the children. Furthermore, the establishment of
34 the trust fund was dependent upon an absolute decree of divorce, as petitioner reserved the power to alter, amend, or revoke in case the divorce was not made final and could have revoked it at any time had the wife not prosecuted her suit to a successful conclusion. This is inconsistent with petitioner's contention that the establishment of the trust was an independent property settlement separate and apart from any obligation to support growing out of the marriage relationship.

Petitioner argues that as the court by its decree only ordered the husband to pay $35,000 per year to the wife during her life, as provided in the separation agreement, and did not specifically order the payments to be made under the trust, the payments of income under the trust were not intended for alimony and support. Payments of income from the trust were to be made by the trustee in accordance with the terms of the trust instrument, and approval of the separation agreement in which was incorporated the trust instrument, in effect, carries with it approval of the payments to be made for the purposes provided in the trust agreement, hence no necessity existed for specific reference in the decree for payment of the trust income for the support and maintenance of the wife and minor children.

A husband has a legal obligation for the support and maintenance of his wife and minor children, and in New York the courts will enforce an agreement for alimony entered into between husband and wife prior to divorce, Daggett v. Daggett, 5 Paige, 509; 28 Am. Dec. 442; Hamlin v. Hamlin, 230 N. Y. S. 51.
35 This legal obligation arises from the relation of mar-

riage. This general obligation for support and maintenance is made specific by the decree of the court of appropriate jurisdiction. Audubon v. Shufeldt, 181 U. S. 575; Romaine v. Chauncey, 129 N. Y. 566; 29 N. E. 826. Agreement between the parties for support and maintenance executed during the pendency of the divorce proceeding, incorporated in the decree, becomes merged in the judgment, Kunker v. Kunker, 246 N. Y. S. 118. The decree of the court for the future maintenance and support of the wife may be in the form of annual payments of alimony or a part of the husband's estate. Gould v. Gould, 245 U. S. 151. The establishment of a trust fund does not destroy the effect of the payments being for support and maintenance. Mary R. Spencer; 20 B. T. A. 58.

Douglas v. Willcuts, 296 U. S. 1, involved a trust quite similar to the one here. A trust fund was set up a few days before the wife obtained a divorce, the income from which was to be used for the purpose of paying alimony. It was held that as the income of the trust was to be used for that purpose the husband received the benefit of the trust income in discharge of his legal obligation to support and maintain his wife and the income was taxable to him.

The Supreme Court held a settlor of a trust taxable with the trust income where it was used to pay his debts in Helvering v. Blumenthal, 296 U. S. 552, in reversing the Second Circuit (76 Fed. (2d) 507), and where it was used to discharge his obligation to maintain and support his minor children in Helvering v. 36 Schweitzer, 296 U. S. 551, in reversing the Seventh Circuit (75 Fed. (2d) 702), and in Helvering v. Stokes, 296 U. S. 551, in reversing the Third Circuit (79 Fed. (2d) 256), and where the beneficiary of a trust irrevocably assigned a part of the trust income to his wife who subsequently obtained a divorce in which the decree made no provision for alimony in Helvering v. Coxey, 297 U. S. 694, in reversing the Third Circuit (79 Fed. (2d) 661).

These decisions are predicated on Douglas v. Willcuts, supra, and establish the proposition that where the income of a trust is to be used in discharge of any legal obligation which the settlor would otherwise have to satisfy, the settlor is taxable with such income to the same extent as if it were personally received.

See also Helvering v. Grosvenor, 85 Fed. (2d) 2; Commissioner v. Hyde, 82 Fed. (2d) 174; Albert C. Whitaker, 33 B. T. A. 865.

In Helvering v. Brooks, 82 Fed. (2d) 173, the Second Circuit had before it an irrevocable trust, created the day before the divorce decree was granted. The decree made no provision as to alimony or property rights of the wife. It was stipulated, however, that the husband and wife had agreed upon the trust indenture as a settlement of their property rights "arising from

the relationship of marriage." The taxpayer sought to make a distinction between an agreement to pay alimony and an agreement for settlement of property rights. In reversing the Board of Tax Appeals and holding the income taxable to the husband, the court said:

37 "* * * Whether the trust income is used to discharge the husband's duty, made specific by agreement, to support the wife, or to discharge an obligation to pay her agreed sums for a release of rights in his property, cannot be material in determining the taxability of the husband. The creation of a trust the income of which is to be used to discharge any legal obligation of the settlor enables him to enjoy the benefit of the income; hence the income is properly taxable to him. Compare Helvering v. Blumenthal, 296 U. S. 552, 56 S. Ct. 305, 80 L. Ed. —; Helvering v. Schweitzer, 296 U. S. 551, 56 S. Ct. 304, 80 L. Ed. —; Helvering v. Stokes, 296 U. S. 551, 56 S. Ct. 308, 80 L. Ed. —; Helvering v. Coxey, 297 U. S. —, 56 S. Ct. 498, 80 L. Ed. —; all of which have been recently decided on the authority of Douglas v. Willcuts. Indeed, in the Douglas Case itself the trust provisions for the wife were in settlement not only of alimony but also 'of any and all dower rights or statutory interests in the estate' of the husband, and the court pointed out (296 U. S. 1, at page 8, 56 S. Ct. 59, 62, 80 L. Ed. —) that this did not affect the essential quality of the payments.

"On the authority of the cases above cited, the order of the Board is reversed."

Petitioner cites and relies on the case of Commissioner v. Tuttle, 89 Fed. (2d) 113, as controlling here. There an irrevocable trust was set up by the husband as a property set-

38 tlement which included settlement and discharge of all claims of the wife for alimony, support, and maintenance of the wife and a complete settlement of all property rights forever under all circumstances and regardless of the outcome or disposition of the divorce proceeding by the wife then pending against her husband. In the instant case the trust was conditioned on a final decree severing the marriage relation. The reservation of the power to amend or revoke in the event the divorce was not made final or the divorce proceeding was discontinued or dismissed, or to change or amend with his wife's consent after the decree became final, destroys the argument of petitioner that the trust was an independent property settlement having no connection with his marital obligation to support and maintain his wife.

The effect of the creation of the trust was the appropriation of a portion of petitioner's property for the uses and purposes specified in the trust instrument the income from which, inso-

far as it was payable for the maintenance and support of the wife and minor children, was in discharge of an obligation of petitioner existing at that time. This obligation was made permanent by the decree of the divorce when it was approved and affirmed and incorporated in the decree as a part of the separation agreement.

Petitioner argues that he completely divested himself of all interest in the trust corpus and income and as no part would ever revert to him, the income is not taxable to him as income used to discharge his legal obligation. Petitioner did not
39 part with all present interest. Under the facts and circumstances here the income distributed was charged with serving a beneficial use of the grantor, i. e., a partial discharge of his legal obligation for the support and maintenance of his wife arising by reason of the marriage relation and the support and maintenance of his minor children by reason of his parental obligation. Furthermore, he had the power with the consent of his wife to change or amend the trust agreement after the decree of divorce became final, and it is an established fact that he did exercise this power on three separate occasions. We are of the opinion and hold that the income of the trust distributed during the taxable year, except that portion paid to Jeanne Leonard in the amount of $2,083.33, is taxable to petitioner. Robert Glendinning et al., Executors, 36 B. T. A.—(No. 82).

The undistributed portion of the income received during the taxable year is not taxable to petitioner, E. E. Black, 36 B. T. A. 346; G. C. M. 18972, I. R. B. Vol. XVI—No. 33, p. 6.

Decision will be entered under Rule 50.

40 Before United States Board of Tax Appeals,
Washington

Docket No. 65805

STEPHEN J. LEONARD, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Decision

Pursuant to Findings of Fact and Opinion promulgated in the above-entitled proceeding September 28, 1937, the respondent filed recomputation under Rule 50, in accordance therewith, setting forth a deficiency for the year 1929 of $542.94, to which petitioner filed an acquiescence on November 13, 1937. It is therefore

Ordered and decided, that there is a deficiency for the year 1929 in the amount of $542.94.

Enter.

[SEAL] (Signed) WILLIAM W. ARNOLD,
Member.

41 In United States Circuit Court of Appeals for the Second Circuit

[Title omitted.]

Commissioner's petition for review and assignments of error.

To the Honorable Judges of the United States Circuit Court of Appeals for the Second Circuit:

Now comes Guy T. Helvering, Commissioner of Internal Revenue, by his attorneys, James W. Morris, Assistant Attorney General, J. P. Wenchel, Chief of Counsel, Bureau of Internal Revenue, and George R. Sherriff, Special Attorney, Bureau of Internal Revenue, and respectfully shows:

I

That he is the duly appointed, qualified, and acting Commissioner of Internal Revenue, appointed and holding his office by virtue of the laws of the United States; that Stephen J.
42 Leonard, respondent on reviews, hereinafter called the taxpayer, filed his return for Federal income tax purposes for the year 1929 with the Collector of Internal Revenue for the Third District of New York, whose office is in the City and State of New York and is within the jurisdiction of the United States Circuit Court of Appeals for the Second Circuit.

II

The nature of the controversy is as follows, to wit:

On June 4, 1929, taxpayer created a trust under which certain securities, stock, and cash were delivered to the United States Trust Company of New York, a corporation, as trustee. The purpose of the trust was to provide support and maintenance for the taxpayer's children and his estranged wife. The trust agreement provides that from the net income the trustee shall distribute $5,000.00 to each of his three children, annually, the balance to be paid to his wife for her support and maintenance and, in her discretion, the balance might be used for the support, maintenance, and education of said children. Under the trust agreement it is provided that the beneficiaries shall be paid in

equal monthly installments as far as practicable. Two of said children were minors and one was an adult during the time here involved.

At the time the trust agreement was entered into the taxpayer and his wife were contemplating divorce proceedings. His wife obtained a decree of divorce which became final on October 22, 1929, and in said decree the aforesaid trust
43 agreement was approved and made a part of the judgment of the Court and a further provision for alimony was made in said decree.

From June 4, 1939, to December 31, 1929, the trustee received net income in the amount of $16,191.34. From this sum, during the year 1929, the trustee distributed to the beneficiaries as follows: $5,200.00 to the taxpayer's wife, $2,083.33 was paid directly to the adult child; to each of the minor children $2,083.33, which amounts were paid to their mother as guardian for their account. A balance of $4,741.35 remained undistributed in the hands of the trustee until after the close of the year 1929.

None of the income to the trust was included in the income tax return of the taxpayer for the calendar year 1929. The Commissioner proposed a deficiency for the year 1929 based upon the inclusion of all of the net income of the trust in taxpayer's income and sent taxpayer a notice of deficiency.

III

The taxpayer appealed said determination of the Commissioner to the United States Board of Tax Appeals. The Board, after hearing, held that the income of the trust which was actually distributed to or for the account of the wife and the two minor children is taxable to the taxpayer; that the amount actually distributed to the adult child is not taxable to the taxpayer; and that the undistributed portion of income received by the trustee during the taxable year is not taxable to the taxpayer.
44 The Board ordered and decided that there was a deficiency of but $542.94 for 1929 instead of the deficiency of $3,270.27 proposed by the Commissioner. The Board's findings of fact and opinion were promulgated September 28, 1937, and its final order of redetermination adjudging that there was a deficiency in tax as above stated was entered November 23, 1937.

IV

That the Commissioner, being aggrieved by the conclusions of law and findings of fact made by the Board of Tax Appeals in its said report and also by said order of redetermination, desires to obtain a review of said report and order by the United States

Circuit Court of Appeals for the Second Circuit and as reasons for such review he alleges that the Board, in rendering its opinion and entering its final order of redetermination, committed the following errors:

1. The Board erred in holding that the undistributed portion of the income received during the taxable year is not taxable to the taxpayer.

2. The Board erred in holding that the undistributed portion of the income received during the taxable year, later to be distributed to the wife and the minor children of the taxpayer, is not taxable to him.

3. The Board erred in failing to hold that the undistributed portion of the income received during the taxable year, later to be distributed to the wife and the minor children of the taxpayer, is taxable to him.

45 4. The Board erred in failing to hold that the undistributed portion of the income received during the taxable year was currently distributable towards support and maintenance of the taxpayer's wife and minor children.

5. The Board erred in failing to sustain the Commissioner's determination.

6. In entering judgment the Board erred in failing to include in taxpayer's taxable income the undistributed income received by the trust during the taxable year and held for later distribution to taxpayer's wife and minor children.

Wherefore, the Commissioner petitions that said report and decision of the United States Board of Tax Appeals be reviewed by the Circuit Court of Appeals for the Second Circuit; that a transcript of the record be prepared in accordance with the law and the rules of said Court and be transmitted to the Clerk of said Court for filing and that appropriate action be taken to the end that the errors herein complained of may be reviewed and corrected by said Court.

JAMES W. MORRIS,
Assistant Attorney General.
(Signed) J. P. WENCHEL.
J. P. Wenchel,
Chief Counsel,
Bureau of Internal Revenue.

Of Counsel:
(Signed) GEORGE R. SHERRIFF.
George R. Sherriff,
Special Attorney,
Bureau of Internal Revenue.

46 [*Duly sworn to by George R. Sherriff; jurat omitted in printing.*]

47 In United States Circuit Court of Appeals, for the Second Circuit

[Title omitted.]

Notice of filing petition for review

To STEPHEN J. LEONARD,
465 Park Avenue, New York, New York.

You are hereby notified that the Commissioner of Internal Revenue did, on the 9th day of February 1938, file with the Clerk of the United States Board of Tax Appeals, Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Second Circuit, of the decision of the Board heretofore rendered in the above-entitled case. Copies of the petition for review and the assignments of error as filed are hereto attached and served upon you.

Dated, this 9th day of February 1938.

(Signed) J. P. WENCHEL,
J. P. Wenchel,
Chief Counsel,
Bureau of Internal Revenue.

48 Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this 10th day of February 1938.

(Signed) STEPHEN J. LEONARD,
Stephen J. Leonard,
Respondent on review.

In United States Circuit Court of Appeals, for the Second Circuit

[Title omitted.]

Notice of filing petition for review

To J. DONALD DUNCAN, *Esq.*,
50 Broadway, New York, New York.

49 You are hereby notified that the Commissioner of Internal Revenue did, on the 9th day of February 1938, file with the Clerk of the United States Board of Tax Appeals, Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Second Circuit, of the decision of the Board heretofore rendered in the above-entitled case. Copies of

the petition for review and the assignments of error as filed are hereto attached and served upon you.

Dated this 9th day of February 1938.

(Signed) J. P. WENCHEL,
J. P. Wenchel,
Chief Counsel,
Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this 9th day of February 1938.

(Sgd.) J. DONALD DUNCAN,
Attorney for respondent on review.

50 Before United States Board of Tax Appeals

[Title omitted.]

Petition of taxpayer for review

Taxpayer, the petitioner in this case by J. Donald Duncan, Counsel, hereby files his petition for a review by the Circuit Court of Appeals for the Second Circuit of the decision by the United States Board of Tax Appeals rendered on November 23, 1935, 36 B. T. A. —, No. 95, determining a deficiency in the petitioner's federal income taxes for the calendar year 1929 in the amount of $542.94 and respectfully shows:

I

The petitioner, Stephen J. Leonard, is an individual residing at 1067 Fifth Avenue, New York, N. Y.

51 II

NATURE OF CONTROVERSY

The controversy involves the proper determination of the petitioner's liability for federal income taxes for the calendar year 1929.

On June 4, 1929, the petitioner entered into two agreements, as follows:

1. A Separation Agreement between petitioner and his former wife, Adelaide Shanahan Leonard, which provided for the payment by petitioner of the sum of $35,000 per year for the main-

tenance and support of said petitioner's former wife and their three children and the payment by petitioner of extraordinary medical expenses of said former wife and children.

2. A Trust Agreement between petitioner, Adelaide Shanahan Leonard and United States Trust Company of New York by the terms of which Agreement both the petitioner and the said Adelaide Shanahan Leonard deposited certain property with the United States Trust Company of New York, in trust, and out of the income from said Trust, the sum of $5,000 was to be paid to each of petitioner's three children; such payments to be made to petitioner's former wife Adelaide Shanahan Leonard during the minority of any of said children and the balance of such income to be paid to the petitioner's former wife, Adelaide Shanahan Leonard. That said Trust Agreement provided that
52 upon the death of said petitioner's wife, the entire income from the Trust was to be paid to the then living children of the petitioner by said wife in equal shares during their lives and the principal of the trust fund to be paid upon the death of each child to such parties as the child in its Last Will and Testament might direct and in default of such appointment to the child's issue and in default of such issue to the other descendants of the petitioner by his said wife, or if there were no such descendants then to the descendants of the petitioner.

Thereafter, and on or about October 22, 1929, a final decree of divorce was entered in the Supreme Court of the State of New York, granting unto petitioner's former wife, Adelaide Shanahan Leonard, a decree of absolute divorce. The foresaid decree approved and affirmed the first of the above mentioned agreements, namely, the Separation Agreement between petitioner and Adelaide Shanahan Leonard and directed the payment by petitioner to Adelaide Shanahan Leonard of the sum of $35,000 per year.

The Commissioner of Internal Revenue under letter dated March 11, 1932, asserted a deficiency in petitioner's income tax for the year 1929 of $3,270.27 based on the proposed addition to petitioner's income for the year 1929 of the amount of income received by the United States Trust Company of New York, as Trustee of the aforesaid Trust and the inclusion in the petitioner's income of the amount of capital gains on securities sold by said Trustee.

53 The Commissioner of Internal Revenue attempted to include the aforesaid income in petitioner's return for the year 1929 on the theory that such payments were made in discharge of petitioner's obligation to support and maintain his wife and minor children.

That the Board of Tax Appeals has determined that the cash payments made to petitioner's wife and minor children during the year 1929 by the Trustee of the aforesaid Trust Agreement represented income to petitioner and as such was taxable to him.

III

The said taxpayer being aggrieved by the findings of fact and conclusions of law contained in the said findings and opinion of the Board, and by its decision entered pursuant thereto, desires to obtain a review thereof by the Circuit Court of Appeals for the Second Circuit.

IV

ASSIGNMENT OF ERRORS

The petitioner assigns as error the following acts and omissions of the Board of Tax Appeals:

1. The finding of the Board of Tax Appeals that the amount of income earned by the Trust created by petitioner and his wife on June 4, 1929, and paid to petitioner's former wife and infant children during the calendar year 1929 was income to petitioner and as such was taxable to him.

54 2. The failure to find that the Trust Agreement created by petitioner and his wife on June 4, 1929, was a voluntary act of the petitioner and his wife and that the same was not directed to be made by the decree of the New York Supreme Court awarding a final decree of divorce to petitioner's former wife Adelaide Shanahan Leonard.

3. The holding that the Trust Agreement of June 4, 1929, was approved and confirmed by the decree of divorce obtained by petitioner's former wife, Adelaide Shanahan Leonard.

4. The holding that the Trust Agreement was created in order to provide suitable provision for the support and maintenance of petitioner's former wife and minor children in fulfillment of a legal obligation imposed on petitioner to support said former wife and minor children.

5. The failure to find that the decree of divorce obtained by petitioner's former wife which provided for the payment of $35,000 per year alimony was the only amount which petitioner was directed by the decree of divorce to pay petitioner's former wife and minor children for their support and maintenance.

6. The failure to find that the petitioner divested himself of all interest in the Trust corpus and income and that said Trust Agreement constituted an irrevocable trust under the income tax laws.

7. The failure to find that the Supreme Court of New
55 York had no authority to direct the taxpayer to create a trust or require taxpayer to set aside any portion of his property for the maintenance of his former wife and minor children.

8. The finding of a deficiency for the year 1929 in lieu of a determination that the income actually received by petitioner for the year 1929 was the total amount of taxable income received by the taxpayer during said year.

J. DONALD DUNCAN,
Counsel for Petitioner,
50 Broadway, New York, N. Y.

[*Duly sworn to by J. Donald Duncan; jurat omitted in printing.*]

56 Before United States Board of Tax Appeals

[Title omitted.]

Notice of filing petition for review

To JOHN P. WENCHEL,
Chief Counsel, Bureau of Internal Revenue, Washington, D. C.

Please take notice that the petitioner on the 14th day of February 1938 filed with the Clerk of the United States Board of Tax Appeals at Washington, D. C., a petition for review by the Circuit Court of Appeals for the Second Circuit of the decision of the Board heretofore rendered in the above entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated, New York, N. Y., this 14th day of February 1938.

Respectfully,

J. DONALD DUNCAN,
Counsel for Petitioner,
50 Broadway, New York, N. Y.

57 Personal service of the foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this 14th day of February 1938.

J. P. WENCHEL,
Chief Counsel, Bureau of Internal Revenue,
Counsel for Respondent.

Before United States Board of Tax Appeals

Docket No. 65805

STEPHEN J. LEONARD, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

STEPHEN J. LEONARD, RESPONDENT

Statement of evidence

The following is a statement of evidence and exhibits submitted to the Board of Tax Appeals in the above-mentioned
58 cases so far as is necessary to the assignments of error as filed reduced to narrative form.

This case came on for hearing before Honorable William W. Arnold, a Member of the United States Board of Tax Appeals, at 10:15 A. M. on the 15th day of February 1937. There were present: J. Donald Duncan, Esq., on behalf of the Taxpayer, and Dean P. Kimball, Esq., on behalf of the Commissioner.

Statement of facts

1. On June 4, 1929, Taxpayer and his former wife, Adelaide Shanahan Leonard, executed a Separation Agreement (Exhibit No. 1 hereof).

2. On June 4, 1929, Taxpayer created a Trust and delivered certain securities, stock, and cash to the United States Trust Company of New York as Trustee under the Trust Agreement (Exhibit No. 2 hereof).

3. At the time of the execution of the Separation Agreement and Trust Agreement, Taxpayer and his former wife were contemplating divorce proceedings.

4. By a decree of the Supreme Court of the State of New York, County of New York, Adelaide Shanahan Leonard, Taxpayer's wife, obtained a decree of divorce from Taxpayer which decree became final on October 22, 1929 (Exhibit No. 3 hereof).

5. During the taxable year 1929 the United States Trust
59 Company of New York as Trustee under the Trust Agreement of June 4, 1929, received net income of $16,191.34 and from such sum the Trustee during the year 1929 made the follow-

ing distributions: Adelaide Shanahan Leonard, Taxpayer's wife, $5,200.00, Adelaide Shanahan Leonard for Craigh Leonard, a minor, $2,083.33, Adelaide Shanahan Leonard for Stephanie Leonard, a minor, $2,083.33; and to Jeanne Leonard, an adult, $2,083.33. This left a balance of $4,741.35 on hand at the close of the calendar year which was not distributed by the Trustee. None of said net income received by the Trustee was reported in the Taxpayer's return for the year 1929.

6. The Trust Agreement of June 4, 1929 was amended on three occasions (Exhibits Nos. 4, 5, and 6 hereof).

7. Stephen J. Leonard testified that at the time of the execution of the Trust Agreement Adelaide Shanahan Leonard was worth between $400,000 and $500,000 which amount she had received as gifts from Stephen J. Leonard and in addition held three life insurance policies in the sum of $100,000 each, which had been transferred to her irrevocably by Stephen J. Leonard. The three policies of insurance were contributed by Adelaide Shanahan Leonard to the Trust Fund created by Agreement of June 4, 1929 and subsequently were surrendered by the trust estate and the cash surrender value thereof amounting to $54,640 became part of the principal of the Trust.

60 8. Lloyd A. Waugh, Assistant Comptroller, United States Trust Company of New York, Trustee under the Trust Agreement of June 4, 1929, on redirect examination testified in response to questions by counsel for Stephen J. Leonard, as follows:

By Mr. DUNCAN:

Q. When you said you made the payments to Adelaide Leonard of the amounts you had referred to for the two minors, you meant you paid them to her for the account of the children, did you not?—A. That is true.

Q. Can you explain Paragraph 8 (a) at page 13 of the original trust agreement which reads as follows:

"From the net income of the trust fund during the life of the third party, the wife of the grantor, at the date of the execution of this agreement, the trustee shall pay to each of the following three named children of the third party by the grantor (namely Jeanne Leonard, Stephanie Leonard, and Craigh Leonard) the sum of $5,000 per year except that during the minority of each of said children, the $5,000 payable to said minor shall be paid to the third party as the natural guardian of and for the account of such minor child; * * *"

Do you know why the entire income, with the exception of the excess over $15,000, was not paid to the three children?—A. I cannot say.

61 Q. You do not know who fixed the amount with the exception of the amount paid to the children?—A. I know that comes in the Remittance Department, but I know that is not the way we reported that for income tax purposes. We reported it for the benefit of the children, each $5,000.

Mr. DUNCAN. That is all.

9. Stephen J. Leonard testified in response to questions by his counsel, as follows:

By Mr. DUNCAN:

Q. Now, Mr. Leonard, there has been introduced in evidence Petitioner's Exhibit No. 1, the separation agreement, and Petitioner's Exhibit No. 2, the trust agreement. Take your time in answering, because I assume the Government will object. Why were there two different documents used?—A. Why?

Q. Yes.—A. Well, the separation agreement, as I said, carried alimony for a period of years, and the other document was for the trust fund which was used for the benefit of the children.

Mr. KIMBALL. I move that that be stricken. That is incompetent; the instruments speak for themselves.

The MEMBER. Motion denied.

Mr. KIMBALL. Exception.

The MEMBER. Noted. The evidence will be considered; if it is immaterial, its admission will not hurt anything.

62 By Mr. DUNCAN:

Q. You have testified, I think, of the amount that your wife was worth at the time of the divorce but I do not think you stated whether any of the amount was real estate, and how much was personal property; will you please explain?—A. Well, I am sure that the securities that she had in her possession at the time that the trust fund was created for the children amounted to between four and five hundred thousand dollars in securities. They were important, they were my gilt-edge securities. In addition to that, she owned my country home which was worth about $200,000.

Mr. KIMBALL. Had you given her these securities?

The WITNESS. Well, when the divorce was first suggested, I was carrying accounts in her name and also accounts in my name, and I gave her all of the securities prior to the papers that were signed for herself, and then I set up a trust fund for the children of approximately $650,000. In other words, my intent was to divide my fortune; she was to get one-quarter, the children another quarter, and I was to get the other half.

The foregoing constitutes all of the evidence pertinent to the assignments of error in these proceedings for review.

J. DONALD DUNCAN,
Attorney for Stephen J. Leonard.
J. P. WENCHEL,
Chief Counsel for the Bureau of Internal Revenue.

63 The foregoing Statement of Evidence is hereby approved and signed and ordered to be made part of the record in the above-entitled proceedings this — day of March 1938.

WILLIAM W. ARNOLD,
Member, United States Board of Tax Appeals.

Exhibit 1, annexed to foregoing statement of evidence

SEPARATION AGREEMENT BETWEEN ADELAIDE SHANAHAN LEONARD AND STEPHEN J. LEONARD, JUNE —, 1929

This agreement, made this 4th day of June 1929, between Adelaide Shanahan Leonard, hereinafter designated as the first party, and Stephen J. Leonard, hereinafter designated as the second party, witnesseth,

Whereas, the first party and the second party were duly married on or about the 17th day of April 1906, in the city, county, and State of New York, and the issue of such marriages

64 are two daughters, Jeanne Leonard, now of the age of twenty-one years; Stephanie Leonard, now of the age of seven years; and a son, Craigh Leonard, now of the age of nineteen years, and

Whereas, unhappy and irreconcilable differences have arisen between the parties hereto as a result of which the parties hereto have been and are now living separate and apart; and

Whereas, the parties hereto desire to enter into an agreement by the terms of which they may hereafter continue to live separate and apart and by the terms of which proper and reasonable provision shall be made for the maintenance and support of the party of the first part and the maintenance, support, and custody of the aforesaid two daughters and son; and

Whereas, by separate Trust Agreement bearing even date herewith by and between second party as Grantor and United States Trust Company of New York, of 25 Wall Street, Borough of Manhattan, City and State of New York, as Trustee, some provision has been made by the second party for the maintenance and support of the first party and the aforesaid two daughters and son, which Trust Agreement is incorporated

herein by reference thereto as though fully and at length set forth, and is marked Exhibit A.

Now, therefore, it is hereby mutually agreed as follows:

65 First. That from and after the date hereof, the parties hereto may and shall continue to live separate and apart from each other, as if the parties hereto were unmarried; that each party hereto shall be free from the control and authority of the other party; and that each party hereto may reside at such place or places as such party shall deem proper.

Second. That neither party shall in any manner annoy, molest, or otherwise interfere with the other party hereto in his or her personal affairs and business, nor shall either party hereto, at any time, institute or cause to be instituted any action, proceeding, or suit to compel the other party hereto to cohabit with him or her: nor, so long as the parties hereto shall both respectfully fulfill their obligations each to the other as herein set forth, shall either party hereto sue or suffer the other to be sued in any action for separation for living separate and apart from the other party.

Third. Second party has in the aforesaid Trust Agreement (Exhibit A) established a Trust Fund with a principal of Four Hundred Thousand Dollars ($400,000.00) principal amount of McCulloch Oil Company of Delaware, Three-Year, 6% First Mortgage Sinking Fund Gold Bonds of March 1, 1929, and Two Hundred Fifty Thousand Dollars ($250,000.00) in cash or other securities, the net income of which trust is payable to the first party subject to a prior charge of Fifteen Thousand Dollars ($15,000.00) in favor of the three children of the parties

66 hereto. In addition to the establishment of the aforesaid Trust Fund, first party has received in the past by way of gifts from the second party personal property which now has the value of at least Three Hundred and Fifty Thousand Dollars ($350,000.00) which is hereby confirmed by first party to have a present income value of at least Fifteen Thousand Dollars ($15,000.00), so that first party hereby agrees that she as of the date of the execution of this Agreement has an income of at least Thirty Thousand Dollars ($30,000.00) a year from the aggregate net income of the property given to her by her husband and from the aforesaid Trust Fund (Exhibit A), subject only to the necessity to provide therefrom for the support of the first party and the support, maintenance, and education of the aforesaid three children. Inasmuch as the Trustee of the aforesaid Trust Fund will not be able immediately upon execution of the said Trust Agreement to begin payment to the beneficiaries of the full amount of income which the Trust Fund will permit when and as the Trustee receives said income, the Second Party

hereby agrees that he will make the following payments to First Party in addition to the payments hereinafter mentioned in subparagraph (c) of this Article Third: viz,

(a) on July first and on August first, 1929, the sum of Twenty-Five Hundred Dollars ($2,500.00);

(b) in addition from and after September first, 1929, until ten days after Second Party shall have withdrawn from the Trust Fund the eleven hundred (1,100) shares of the capital stock of the Bankers' Trust Company of New York and paid into the Trust Fund in place thereof the sum of $149,600.00 in cash, interest at the rate of five (5) per centum per annum, on the said $149,600.00 represented by said shares of the said Bankers' Trust Company of New York, to be calculated and paid to First Party quarterly beginning December first, 1929, and against and from which quarterly payment Second Party shall credit himself and deduct the amount of any dividends which may be paid after the date of the execution of said Trust Agreement to the Trustee by the said Bankers' Trust Company of New York upon any of said shares deposited in said Trust Fund;

67

(c) in addition to the payments mentioned in subparagraphs (a) and (b) of this Article third, second party hereby agrees to pay to first party for the support and maintenance of first party and the aforesaid three children of the parties hereto,

(i) on the fifteenth day of June in each year beginning with the year 1929, the sum of Ten Thousand Dollars ($10,000.00);

(ii) and in addition thereto, the sum of Twenty-Five Thousand Dollars ($25,000.00) per year to be paid so far as may be arithmetically possible in equal monthly payments on the first day of each month beginning with the month of July 1929.

68

Second party shall continue to pay to First Party the aggregate sum of Thirty-Five Thousand Dollars as specified in (i) and (ii) above, each year during the life of first party, provided second party's circumstances and ability to pay the said Thirty-five Thousand Dollars ($35,000.00) continue to be as good or better than as of the date of the execution of this Agreement making the aggregate net income receivable by first party to be used by her for her maintenance and support and that of the aforesaid three children, approximately Sixty-five Thousand ($65,000.00) per year, from

Property represented by gifts received heretofore from second party; the aforesaid Trust Fund (Exhibit A), and the aforesaid yearly payment of Thirty-five Thousand Dollars ($35,000.00).

Second party shall not in any way be responsible for any diminution of the net income receivable by the First Party by reason

of any decrease in income from the property heretofore given to First Party by Second Party or from the Trust Fund, as referred to in this section, exc'pt as otherwise provided in the Trust Fund (Exhibit A) with r'spect to the Bonds of the McCulloch
69 Oil Company of Delaware. In addition to the aforesaid Thirty-five Thousand Dollars ($35,000.00) per year, second party hereby agrees to pay any extraordinary medical or surgical expenses incurred by first party or on behalf of the aforesaid three children until the time when each child respectively shall attain the age of twenty-five years. In the event that the ability of the party of the second part to pay the aforesaid Thirty-five Thousand Dollars ($35,000.00) shall be impaired, second party shall have the right to apply to any court of competent jurisdiction for a reduction of his obligation to pay the Thirty-five Thousand Dollars ($35,000.00) per year to not less than $10,000.00 per year, and or the extraordinary medical or surgical expenses, provided that no such application shall be made within two years of the date of the execution of this Agreement. If at any time after two years from the date of the execution of this Agreement because of change of financial circumstances or inability to pay the aforesaid Thirty-five Thousand Dollars ($35,000.00), the second party shall have applied to a Court for and shall have been granted a reduction in the Thirty-five Thousand Dollars ($35,000.00) payable to first party as aforesaid and thereafter the financial circumstances of the second party shall improve so that he shall be once more able to pay Thirty-five Thousand Dollars ($35,000.00) per year to the first party, the first party shall at any such time have the right to apply to any Court of competent jurisdiction for an increase in the amount then being paid to the first party by the second party, provided that
70 any increase which may be granted shall never cause the second party to pay to the first party a greater amount in the aggregate than Thirty-five Thousand Dollars ($35,000.00) per year.

Fourth. At the time of the execution of this Agreement the first party has deposited with and assigned to the Trustee of the aforesaid Trust (Exhibit A), policies insuring the life of the second party as follows:

Number of Policies	Amounts	Names of Companies
487591	$100,000.00	Connecticut Mutual Life Insurance Company.
374279	$100,000.00	Aetna Life Insurance Co.
621369	$100,000.00	Massachusetts Mutual Life Insurance Company.

The beneficiary named in the aforesaid policies is the first party of this Agreement. The first party hereby agrees to immediately authorize the beneficiary named in said policies to be changed to and the proceeds thereof to be payable thereafter to

the Trustee then acting as such, pursuant to the terms of said Trust Agreement, but the first party hereby agrees to continue to pay the premiums on said insurance policies as and when they shall become due and payable, and if at any time the first party shall default in paying said premiums, the second party may at his option pay said premiums and deduct the amount thereof from any amount payable to the first party by the
71 second party pursuant to the terms of this Agreement, and the right to such deduction shall be the sole remedy of the party of the second part against the party of the first part by reason of such default.

Fifth. All furniture and fixtures and other personal property, including automobiles, now contained in or appurtenant to the real property and dwellings at East Hampton, Long Island, New York, and the apartment at 420 Park Avenue, New York City, now occupied by the party of the first part, is hereby confirmed to be the personal property of the party of the first part, and the party of the second part hereby releases any and all claim which he may have had therefor.

Sixth. The first party shall at all times from and after the date of this Agreement have the sole care, custody, and control of the aforesaid three children, namely, Jeanne, Stephanie, and Craigh Leonard, provided that the second party shall have the right to visit and see the said children at any and all reasonable times.

Seventh. The first party will submit to the second party a complete statement of all of the outstanding charges for living and other expenses which she has or shall have incurred for herself and for the account of the aforesaid three children up to the first day of the month immediately succeeding the date of the execution of this Agreement which first day of the month is hereinafter referred to as the settlement date, and the second party hereby agrees to pay all of said charges contained in said
72 statement and to begin the payment of the aforesaid Twenty Five Thousand Dollars ($25,000.00) per year as from the said settlement date. From and after said settlement date all charges for living or other expenses of any description whatsoever not contained in the aforesaid statement shall be paid by the first party, except that the second party will pay such charges for living and other expenses of the first party rendered during the period of thirty days after said settlement date for purchases or charges made or incurred prior to said settlement date, and if after the date of the execution of this Agreement the second party shall receive any bills or charges for any expenses not contained in the aforesaid statement, he may at his option pay the same and deduct the amount thereof from the

Twenty-Five Thousand Dollars ($25,000.00) per year which he has agreed to pay to the first party pursuant to paragraph third of this Agreement.

Eighth. The first party hereby accepts the establishment of the Trust Fund (Exhibit A) and the payments to be made by the second party pursuant to this Agreement in lieu of all dower, and hereby releases the second party and his estate from any claim of dower in the property of the second party as now or hereafter constituted.

In witness whereof, the parties hereto have hereunto set their hands and seals as of the day and year first above written.

ADELAIDE SHANAHAN LEONARD. [L. S.]
STEPHEN J. LEONARD. [L. S.]

73 STATE OF NEW YORK,
County of New York, ss:

On this 5 day of June, in the year 1929, before me personally came Adelaide Shanahan Leonard, to me personally known, and known to me to be one of the individuals described in and who executed the within instrument, and acknowledged that she executed the same.

PHISI HERTWOHL,
Notary Public.

Certificate Filed in N. Y. Co. 638. Commission Expires Mar. 30, 1930.

STATE OF NEW YORK,
County of New York, ss:

On this 6th day of June, in the year 1929, before me personally came Stephen J. Leonard, to me personally known, and known to me to be one of the individuals described in and who executed the within instrument, and acknowledged that he executed the same.

CHARLES R. LOWTHERN,
Notary Public, New York County.

N. Y. County Clerk's No. 297, Reg. No. TL153. Bronx County Clerk's No. 35, Reg. No. 3120A. Commission Expires March 30, 1931.

74 *Exhibit 2, annexed to foregoing statement of evidence*

AGREEMENT BETWEEN STEPHEN J. LEONARD, UNITED STATES TRUST COMPANY OF NEW YORK, AND ADELAIDE SHANAHAN LEONARD, JUNE 4, 1929

Agreement made this 4th day of June 1929, between Stephen J. Leonard, now residing at ——— in the Borough of Manhattan,

City, County, and State of New York, hereinafter called the "Grantor," party of the first part, the United States Trust Company of New York, a corporation organized and existing under the laws of the State of New York, having its principal office and place of business at 45 Wall Street, Borough of Manhattan, City, County, and State of New York, hereinafter called the "Trustee," party of the second part, and Adelaide Shanahan Leonard, now residing at 420 Park Avenue, Borough of Manhattan, City, County, and State of New York, hereinafter referred to as "the third party," party of the third part, witnesseth,

1. The Grantor, desiring to establish a trust for the uses and purposes hereinafter set forth, has deposited with the Trus-
75 tee $400,000 principal amount McCulloch Oil Company of Delaware Temporary Three Year 6% First Mortgage Sinking Fund Gold Bonds dated 1929, of which principal amount $250,000 thereof are comprised within Series A, and eleven hundred (1,100) shares of the capital stock of The Bankers Trust Company of New York, having a value agreed and fixed by the parties hereto of $149,600, and in addition $100,400 in cash, making an aggregate principal value of $650,000, hereinafter referred to as the "trust fund." On or before January 1, 1930, the Grantor shall withdraw from the trust fund the aforesaid eleven hundred (1,100) shares of the capital stock of The Bankers Trust Company of New York and substitute and deposit with the Trustee in place thereof one hundred and forty-nine thousand six hundred dollars ($149,600) in cash. In the event that on January 1, 1930, the Grantor has not so withdrawn said shares of The Bankers Trust Company of New York and substituted and deposited therefor the said $149,600 in cash, the Trustee shall sell said shares at private or public sale, without the necessity of giving the Grantor any notice whatsoever of the sale or the time or place thereof, and from the proceeds of the sale thereof, deposit $149,600 in the trust fund and pay over the remainder of said proceeds, if any, less all costs of sale, to the Grantor. The Trustee shall not be liable to the Grantor nor to any beneficiary of the Trust Agreement for any deficiency in the event that the net proceeds of such sale do not
76 amount to $149,600 but nothing herein contained shall prevent any beneficiary from bringing any action against the Grantor to require the Grantor to pay into the Trust Fund the amount of any such deficiency.

2. The Trustee shall manage and administer the trust fund from time to time held by it hereunder; shall collect and receive the income of said trust fund; shall pay over and distribute the net income and the principal thereof as provided in Article 8 hereof. If the said paragraph provides for more than one trust, the term "trust" as used in this Agreement shall mean all the trusts men-

tioned in said Article 8 and each of such trusts. While the Trustee shall not be obligated to follow the advice of the Grantor with respect to any investments, at such times as there may be any funds to be invested and at such other times as the Grantor may deem advisable, the Trustee shall use reasonable efforts to consult with the Grantor with respect to the character of the investments of the trust fund. In addition, when the Trustee shall receive payment of the principal of the aforesaid McCulloch Oil Company of Delaware Bonds, or any part thereof, it shall notify the Third Party of the receipt of said payments and shall invest the proceeds thereof in only such securities as shall be approved in writing by the Third Party, except that if such approval shall not be given by Third Party within 15 days after the mailing to her of a request therefor from the Trustee, it may invest said proceeds in such securities as shall then be legal investments for Trustees in accordance with the laws of New York.

77 3. In so far as practicable, the net income of the trust shall be paid to the life beneficiary, or life beneficiaries, for the time being entitled thereto, in equal monthly installments. Income accrued, but not due and payable to the Trustee at the time of the termination of the life interest of any beneficiary hereunder, shall pass and be payable to the beneficiary or beneficiaries entitled to the next eventual estate, whether it be a life estate or otherwise.

4. If under the provisions of said Article 8 any minor shall become entitled to the principal of any distributive share or sub-share, such distributive share or sub-share shall thereupon vest in such minor absolutely, notwithstanding minority, but during such minority the principal of such share or sub-share shall remain in the care and custody of and be administered by said Trustee, who for the purposes of such administration shall have all of the powers, authority, and discretion granted to the Trustee hereunder. When such minor shall attain the age of twenty-one years, the principal of such share or sub-share shall be transferred and paid over to him or to her together with any accumulations thereof. Nothing in this Article contained shall be construed to prevent the operation of the power of appointments granted to the beneficiaries mentioned in said Article 8.

5. Without in any way limiting by implication or otherwise the powers hereinbefore or hereinafter conferred upon the
78 Trustee, or those conferred upon the Trustee by law, the Trustee is hereby expressly granted the following additional powers, authority, and discretions with relation to any and all property, at any time constituting part of the trust, and whether constituting principal or income thereof, and generally with relation to the management and administration of the

trust, to wit: To sell any such property at public or private sale for cash or on credit, or to exchange the same, on such terms as it may deem advisable; to grant options for the sale or exchange of any such property; to retain any such property as an investment so long as it may deem advisable; to invest and from time to time reinvest any such property in such securities (including shares of so-called Investment Trusts) or other personal property, as it may deem proper, without being limited to the class of securities in which Trustees are or may be hereafter authorized by law to invest trust funds; to participate in any plan of reorganization including consolidation or merger, to deposit any such property under any such plan of reorganization or with any protective or reorganization committee, to delegate to such committee discretionary power with relation thereto, to pay a proportionate part of the expenses of such committee, and any assessments levied under any such plan, and to accept and retain new securities received by the Trustee in pursuance of any such plan; to exercise all conversion, subscription, voting and other rights of whatsoever nature appertaining to any such property, and to pay such sums as it may deem advisable in connection therewith;

79 Also to extend the time of payment of any obligation at any time held by it hereunder, except that no extension of the time of payment of the principal or interest of the mortgage bonds of the McCulloch Oil Company of Delaware may be made without (a) the consent of the third party and (b) the extension of the guarantee of the Grantor or his personal representatives; to retain the corpus of two or more of the trusts created hereunder in one or more consolidated funds in which the separate trusts shall have undivided interests, without making a physical division of the investments of such trusts; to make distribution in kind or in cash, or partly in kind and partly in cash, among the persons entitled to share hereunder, its determination as to the fairness and equality of the distribution and as to the value of the property distributed to be conclusive upon all persons interested in the trust hereby created; to compromise, adjust, settle or submit to arbitration upon such terms as it may deem desirable all claims in favor of or against any trust created hereunder; to determine whether any sinking fund shall or shall not be maintained for the amortization of any premium on any securities in its hands, and the amount of such sinking fund; to borrow money, and to pledge or mortgage any such property; to determine what portion of any stock dividend or of any other extraordinary dividend or distribution constitutes principal or income of any trust created hereunder, and

to add to the principal of such trust such portion of any
80 stock or other extraordinary dividend or distribution as
it shall determine to be principal, and to pay out or distribute as income such portion of any stock or other extraordinary dividend or distribution as it shall determine to be income, such determination to afford full protection to the Trustee;

Also to determine whether any expenses or other moneys paid out by it shall be charged against the principal or income of any trust hereby created, such determination to afford full protection to the Trustee; to cause the securities held by it to be registered in the name of a nominee or in its own name without describing the trust and without thereby increasing or decreasing its liability as Trustee; to appoint agents to act in its behalf, and to delegate to them discretionary power;

Also to pay to any adult beneficiary hereunder any income payable to such beneficiary under the foregoing provisions of this Agreement by causing such income to be deposited to the credit of such beneficiary in a checking account in the name of such adult beneficiary on the books of the main office, or any branch office, of United States Trust Company of New York or in any other account which such adult beneficiary shall from time to time designate by an instrument signed by such adult beneficiary and delivered to the Trustee; in the case of any beneficiary hereunder who shall happen to be a minor or otherwise legally incapable of giving a discharge for a payment to him or to her,
to pay any sum or sums which would otherwise be payable
81 to such beneficiary hereunder, to the guardian of the person or of the property of, to the father or mother of such beneficiary, or to the person with whom such beneficiary is at the time residing, such application or payment by the Trustee as hereinbefore in this paragraph provided to be and constitute a full and sufficient discharge to it in respect thereof with any further receipt (except that so long as the third party shall be living any income payable to any minor child of the Grantor and third party shall be paid to the third party as parent and natural guardian of and for the account of said minor child), and generally to exercise for the benefit of the trust hereby created in respect to any property constituting part thereof, all rights, powers and privileges of every name and nature which might or could be exercised by one owning such property absolutely and in his own right, and to enter into such contracts and execute such written instruments as it may deem advisable in connection with the exercise of the foregoing powers, or any of them, and to include therein such covenants, terms and conditions as to it may seem proper, it being expressly understood and agreed that any and all powers granted to the Trustee under this Agree-

ment shall be exercised by it at such times and in such manner as it in its absolute and uncontrolled judgment shall seem advisable, and that the Trustee shall not be liable for any action taken or omitted by it in good faith hereunder.

82 6. The Grantor hereby guarantees to the Trustee the payment when due of the principal and interest on $400,000, principal amount of the 6% First Mortgage Sinking Fund Gold Bonds of the McCulloch Oil Company of Delaware included in the trust fund. Notice of any default in the payment of any interest on or principal of said bonds shall be given to the Grantor at 20 Pine Street, Borough of Manhattan, City and State of New York (or such other address as the Grantor may hereafter designate in writing) by the Trustee after the occurrence of such default (but the omission or failure to give any such notice shall not relieve the Grantor of his guaranty nor of his absolute obligation to substitute securities in the event of such default, as hereinafter set forth in place of said bonds at any time when called upon by any beneficiary or by the Trustee hereunder) and the Grantor shall thereupon substitute cash or securities with a market value equal to the then principal amount of said bonds, together with cash sufficient to cover the accrued interest, if any, on said bonds. Such substituted securities and the market value thereof are to be satisfactory to the Trustee, but in the event that any securities tendered to the Trustee in substitution for said bonds are not satisfactory to the Trustee, the Grantor may substitute, and the Trustee shall accept in substitution such securities as are at such time legal for the investment of trust funds in accordance with the provisions of the laws of the State of New York and at a market value equal to the mean between the closing bid and asked price thereof on the date immediately preceding the day of substitution.

83 7. (a) Until the time mentioned in sub-paragraph (b-1) of subdivision (b) of this Article, the Grantor hereby expressly reserves the right to amend this instrument and the trust hereby created in any respect whatsoever and as often as desired and also to revoke the same either in whole or in part by an instrument signed by the Grantor and delivered to the Trustee. In case of such revocation, the Grantor shall have and possess again, free and discharged of the trust hereby created, the entire trust fund and accumulated income, if any, then in the hands of the Trustee, but such revocation by the Grantor shall not in any way affect the deposit by the third party of the insurance policies hereinafter mentioned in Article 10 of this Agreement and such insurance policies shall remain deposited with the Trustee as the principal of a life insurance trust established by the third party

as in Article 10 of this Agreement provided for and subject to the following terms and provisions:

(i) Upon the death of the insured, the Trustee shall collect the proceeds of said insurance policies and distribute the income and principal of said proceeds as in Article 8 of this Agreement set forth;

(ii) The premiums upon such insurance policies shall be paid in the manner set forth in subdivision (a) of Article 10 of this Agreement.

No amendment, however, shall be made to this instrument
84 which shall in any way increase the obligations of the Trustee hereunder, or diminish its compensation without its written consent. The Grantor shall make, execute and deliver in due form of law such other and further instruments as the Trustee may deem necessary or requisite to effectuate the purposes hereof.

(b) If at any time the third party shall during her life institute any legal proceeding or action for divorce or for the annulment of her marriage with the Grantor, the following provisions shall become effective:

(b-1) Immediately upon the delivery to United States Trust Company of New York, the corporate Trustee hereunder, of a copy of a Summons and Complaint (with an affidavit of service upon the Grantor annexed thereto) in an action for divorce or annulment of the marriage of the Grantor and the third party, the right of the Grantor to amend or revoke this instrument as permitted by Article 7 hereof shall be suspended forthwith until such time as there shall be delivered to the said United States Trust Company of New York, either (i) a certified copy of a final decree of divorce or annulment of the marriage of the Grantor and the third party, or (ii) a copy of a Stipulation executed by the attorneys for the Grantor and the third party
85 evidencing the fact that the aforesaid action for divorce or annulment of the marriage of the Grantor and the third party has been discontinued, or (iii) a certified copy of an order dismissing the aforesaid action. If during said period of suspension there shall be delivered to United States Trust Company of New York, the corporate Trustee hereunder, a certified copy of a final decree of divorce or annulment of the marriage of the Grantor and the third party, the right of the Grantor to amend or revoke this instrument as permitted by Article 7 hereof shall terminate ipso facto and this instrument shall thereafter be construed, so far as the Grantor is concerned, as an irrevocable Trust Agreement, and the said United States Trust Company of New York shall have no further liability to the Grantor for any reason whatsoever. If during said period of suspension there shall be delivered to the said United States Trust Company of

New York a copy of a Stipulation executed by the attorneys for the Grantor, and the third party evidencing the fact that the aforesaid action for divorce or annulment of the marriage of the Grantor and the third party has been discontinued, or a certified copy of an order dismissing the aforesaid action, the right of the Grantor to amend or revoke this instrument, as permitted by Article 7 hereof, shall immediately resume and be in full force and effect and this instrument shall thereafter be construed
86 as a revocable Trust Agreement with all the rights, powers, and obligations, including the same obligations as in this subdivision (b–1) set forth, in the event that during any period of the operation of this instrument as a revocable Trust Agreement, an action for divorce or annulment of the marriage of the Grantor and the third party should be instituted by the third party and documents be delivered to the said United States Trust Company of New York, in the manner as aforesaid.

(b–2) At any time during the life of this Trust Agreement the Trustee may resign its duties by delivering its written resignation to the Grantor (if he be living and this Agreement shall not have become irrevocable) or (if the Grantor be dead or this Agreement shall have become irrevocable), to the life beneficiaries then receiving income, pursuant to the terms of this Agreement and/or the natural guardian of such life beneficiaries as may be then minors. In the event of the resignation, or disability to act of any Corporate Trustee, a successor corporate Trustee shall be immediately chosen:

(a) By the Grantor, if alive, and this Agreement shall not have become irrevocable, or

(b) If the Grantor be dead, or this Agreement shall have
87 become irrevocable, then by the Surrogate's Court of the County of New York, upon application made by the said United States Trust Company of New York, or any beneficiary, and upon the designation of the successor Trustee, the said successor Trustee shall immediately execute a copy of this Trust Agreement as Trustee and shall thereupon become fully vested with all the rights, trust powers, duties, and obligations of its predecessor or predecessors in the trust with like effect as if originally named as Trustee herein.

(c) Any corporation into or with which the Trustee or any successor Trustee may be merged or consolidated, or any corporation resulting from any merger or consolidation to which the Trustee, or any successor Trustee may be a party, or any corporation in any manner succeeding to the business of the Trustee, or of any successor Trustee, as a whole, or substantially as a whole, shall be the successor of the Trustee under this Trust Agreement without the execution or filing of any instrument, or the per-

formance of any further act on the part of any of the parties hereto, or of the beneficiaries hereunder, anything herein to the contrary notwithstanding.

(d) The Trustee shall not be responsible or liable for any error of judgment, or mistake of law or fact, or for any unwise decision, duty, power, or trust imposed or conferred upon it, hereunder, nor for anything whatever in connection with this Trust Agreement, except for its misconduct or gross negligence. The Trustee and every successor Trustee shall be exempt from giving any bond or surety in respect to the execution of the trust or powers herein contained, or otherwise in respect of the premises.

8. Subject to the terms of Article 10 of this Agreement:

(a) From the net income of the trust fund during the life of the third party, the wife of the Grantor at the date of the execution of this Agreement, the Trustee shall pay to each of the following three named children of the third party by the Grantor (namely, Jeanne Leonard, Stephanie Leonard, and Craigh Leonard), the sum of Five Thousand Dollars ($5,000) per year, except that during the minority of each of said children the Five Thou-

89 sand Dollars payable to said minor shall be paid to the third party as natural guardian of and for the account of said minor child; if any of said children shall die during the life of the third party the Five Thousand Dollars payable to said child who shall so die shall be thereafter payable to the third party during her life for her own separate use; the remaining net income of the trust fund shall be paid to the third party during her life, to be used by her for her maintenance and support and, in her sole discretion, for the support, maintenance, and education of the children, of herself, and the Grantor.

(b) Upon the death of the third party, the principal of the trust fund then in the hands of the Trustee shall be divided into as many equal separate parts as there shall be then living children of the third party by the Grantor and deceased children of the third party by the Grantor leaving issue surviving the third party.

(c) The Trustee shall thereupon set apart and hold one of such equal separate parts in a separate trust fund for the benefit of each living child of the third party by the Grantor, hereinafter designated the life beneficiary thereof, and invest and reinvest each of such parts and collect and receive the rents, issues, income, and profits of each thereof and after paying therefrom the disbursements and charges properly chargeable against the income thereof, to apply to the support, maintenance, and education of the life beneficiary thereof during his or her minority so much of the net rents, issues, income, and profits of the

90 part so held for him or her as said Trustee shall in its

uncontrolled discretion deem proper and to accumulate for his or her benefit during his or her minority any balance thereof and to pay over such accumulations to him or her on his or her attaining the age of twenty-one years and to pay over to him or her from and after attaining the age of twenty-one years in monthly payments for and during his or her life the whole of the net rents, issues, income, and profits of the part so held for him or her; and upon the death of each of such life beneficiaries, whether before or after attaining the age of twenty-one years, to pay over the principal of the part so held for his or her benefit together with any accumulations of the rents, issues, income, and profits thereof that may not previously have been paid hereunder, to such persons or corporations in such shares, interests, estates, and proportions as he or she shall in and by his or her last Will and Testament in that behalf direct, limit, and appoint; or, in default of such appointment on his or her part, to his or her issue him or her surviving per stirpes and not per capita; and if such life beneficiary shall leave no issue him or her surviving, then to the other descendant or descendants then living, of the third party by the Grantor per stirpes and not per capita, if there be any, and if there be no such other descendant or descendants then living, to the descendants of the Grantor per stirpes and not per capita.

(d) One of such separate parts shall be paid over by
91 the Trustee to such persons or corporations as any child of the third party by the Grantor who shall have died before (but leaving issue at the time of) the death of the third party in his or her last will and testament shall have directed, limited or appointed, or in default of such appointment on his or her part to his or her issue him or her surviving per stirpes and not per capita, if there be any, and if there be no such issue then living at the date of the death of the third party, then to the other descendant or descendants then living of the third party by the Grantor per stirpes and not per capita and if there be no such other descendant or descendants than living then to the descendants of the Grantor per stirpes and not per capita.

9. The Trustee shall be entitled to compensation as follows:

Two per cent (2%) of the principal amount of the trust fund to be payable on the date of the termination of said trust, and two and one-half percent (2½%) of income from the trust fund up to $20,000, and one and one-half percent (1½%) of the income in excess of $20,000 payable quarterly or annually at the option of the said United States Trust Company of New York.

10. At the time of the execution of this Agreement, the third

party has deposited with and assigned to the Trustee policies insuring the life of the Grantor, as follows:

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Number of Policies	Amounts	Names of Companies
487591	$100,000.00	Connecticut Mutual Life Insurance Company.
374279	$100,000.00	Aetna Life Insurance Co.
621369	$100,000.00	Massachusetts Mutual Life Insurance Company.

The beneficiary named in the aforesaid policies is the third party. As soon as possible after the execution of this Agreement, the beneficiary named in said policies shall be changed to and the proceeds thereof shall be payable thereafter to the Trustee then acting as such, pursuant to the terms of this Agreement, and shall be held by such Trustee as part of the principal of the trust fund. From and after the time when the Trustee shall become the beneficiary named in said policies, the premiums upon said policies shall be paid in the following manner:

(a) During the life of the third party the premiums shall be paid by the third party to the Trustee at least three days before the due date for the payment of said premiums, and the Trustee shall thereupon pay the said premiums, as and when due to the insurance companies. In default of payment of said premiums by third party as aforesaid, the Trustee shall

93 notify the insured and if the insured shall not immediately pay said premiums, the Trustee and the insured shall immed'ately cause the insurance companies to pay to the Trustee the cash surrender value of said policies as of such time as the payments of said premiums shall cease and to deposit said cash surrender value in and as part of the principal in said trust fund. It shall not be the duty or the right of any party to or beneficiary under this Agreement to compel the payment by the party of the third part of premiums on said insurance policies by legal proceedings, and her failure to pay such premiums shall create no legal liability on her part under the terms of this Agreement, except as herein expressed.

(b) Upon the death of the third party, the premiums on said policies shall be paid as and when due by the Trustee which is hereby authorized to deduct pro rata the amount thereof from the income payable to the then life beneficiaries of the trust fund, except that if the principal of said trust fund shall upon the death of the third party be reduced by any payment over of any principal to any beneficiary so that the remaining principal in the trust fund shall be insufficient to permit of the payment of an income sufficient to pay the amount of said insurance premiums, the trustee shall request the insured to pay

94 said premiums as and when due, and in default of such payment, shall cause the insurance companies to pay the

cash surrender value of said policies as of such time that the payment of said premium shall cease, and to deposit said cash surrender value in and as part of the trust in said trust fund.

11. At the time when Craigh Leonard, the son of the Grantor, shall attain the age of twenty-one years, he shall become a Trustee of this Trust Agreement by executing a copy thereof and filing the same with the corporate Trustee then acting. Upon so becoming a Trustee, the duties of the said Craigh Leonard shall be to consult with the corporate Trustee with respect to the investments of the trust fund, but the decision of the corporate Trustee with respect to said investments, or upon any and all other questions which may arise under the terms of the said Trust Agreement, shall be conclusive. For his services as such Trustee the said Craigh Leonard shall receive a half of one per-cent of the income from the trust fund, per year, payable quarterly.

12. Notwithstanding any of the terms or provisions of Article 7 having to do with the irrevocability of this Agreement, this Agreement or any of the terms thereof may be changed or amended during the lifetime of the Grantor with the consent of the third party. Before such change or amendment
95 shall become effective, an instrument substantially in the form of this Agreement shall be executed by the Grantor and the third party together with the Trustee of this Agreement or such other trustee as may be chosen by the Grantor and the third party and if any change in trustee is made, a copy of the new agreement or amendment shall be filed with the Trustee then acting under the terms of this Agreement and immediately upon such filing, either in the form of a new agreement or as an amendment to this Agreement, the new agreement or the amendments to this Agreement shall be deemed to be effective forthwith. Nothing in this Agreement contained shall be deemed to vest any interest in the children of the third party and the Grantor prior to the death of the Grantor or the third party, and the said children shall have no right to object to any change or amendment of this Agreement which shall be made and/or executed with the consent and under the signature of the third party.

13. The Trustee accepts the trust hereby created and agrees to carry out the provisions thereof on its part.

In witness whereof, the Grantor has hereunto set his hand and seal, the third party has hereunto set her hand and seal and the Trustee has caused its corporate seal to be hereunto affixed and these presents to be signed by one of its Vice-

96 Presidents and attested by its Secretary or one of its Assistant Secretaries, the day and year first above written.

[L. S.] STEPHEN J. LEONARD, *Grantor.*

UNITED STATES TRUST COMPANY OF NEW YORK, *Trustee.*

By: (Illegible) *1st Vice President.*

Attest:

H. B. HENZE, *Assistant Secretary.*

[L. S.] ADELAIDE SHANAHAN LEONARD, *Third Party.*

STATE OF NEW YORK,
County of New York, ss:

On this 6th day of June, in the year 1929, before me personally came Stephen J. Leonard, to me personally known, and known to me to be one of the individuals described in and who executed the within instrument, and acknowledged that he executed the same.

CHARLES R. LOWTHERN,
Notary Public New York County.

N. Y. County Clerk's No. 297, Reg. No. TL153. Bronx County Clerk's No. 35, Reg. No. 3120A. Commission Expires March 30, 1931.

97 STATE OF NEW YORK,
County of New York, ss:

On this 13 day of June, in the year 1929, before me came W. Pell, to me known, who, being by me duly sworn, did depose and say that he resides in Rye, New York; that he is the First Vice President of United States Trust Company of New York, the corporation described in and which executed the above instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by order of the Board of Trustees of said corporation, and that he signed his name thereto by like order.

N. A. MULLINS,
Notary Public, Kings County No. 744.

Cert. Filed in New York Co. No. 743. New York Co. Reg. No. 1-M-496. Kings Co. Reg. No. 1339. Commission Expires March 30, 1931.

STATE OF NEW YORK,
County of New York, ss:

On this 5th day of June, in the year 1929, before me personally came Adelaide Shanahan Leonard, to me personally known, and known to me to be one of the individuals described in and who executed the within instrument, and asknowledged that she executed the same.

PHISI HERETWOHL,
Notary Public, Kings Co.

Certificate Filed in N. Y. Co. 638. Commission Expires Mar. 30, 1930.

98 *Exhibit 3, annexed to foregoing statement of evidence*

At a Special Term, Part I, of the Supreme Court, of the State of New York, held in and for the County of New York, at the County Court House in the Borough of Manhattan, City of New York, on the 19th day of July 1929.

Present, Honorable WILLIAM T. COLLINS, Justice.

ADELAIDE S. LEONARD, PLAINTIFF

v.

STEPHEN J. LEONARD, DEFENDANT

The above-entitled action having been brought on by the plaintiff for a judgment of divorce in favor of the plaintiff and against the defendant dissolving the marriage heretofore existing between the parties hereto upon the ground of the adultery of the defendant at the time or times and place or places set forth in the complaint herein, and the defendant having duly appeared herein by Marshall & Auchincloss, Esqrs., his attorneys, and the Court having by its order of reference referred the cause to Honorable George Gordon Battle as Referee to inquire and

99 report the issues in this action, and testimony having been heard on the 1st and 9th days of July 1929, before the said Referee sustaining the allegations set forth in the complaint, and also that there is issue of said marriage, to wit, Jeanne Leonard aged twenty-one years, Craig Leonard aged twenty years, and Stephanie Leonard aged seven years, and also that there is no judgment or decree in any Court of this State of competent jurisdiction against the plaintiff and in favor of the defendant for divorce on the ground of adultery, and that there is no judgment or decree of divorce between the parties hereto rendered by any court having jurisdiction to grant the same in any state, territory, or dependency of the United States or in any foreign country, and the same Referee having heard and considered the proofs offered and having made a report in

writing separately stating the facts found and the conclusions of law deciding that the plaintiff is entitled to a judgment against the defendant dissolving the marriage heretofore existing between the parties hereto pursuant to statute because of the adultery of the defendant, and motion for judgment on the Referee's report having regularly come on at Special Term, Part 1, of this Court on the 17th day of July 1929.

Now on motion of Jackson, Fuller, Nash & Brophy, attorneys for the plaintiff, it is

Ordered, adjudged, and decreed that the report and findings of the Referee herein be and the same are hereby confirmed;

100 Ordered, adjudged, and decreed that the plaintiff is entitled to a judgment that the marriage heretofore existing between the plaintiff and the defendant be dissolved by reason of defendant's adultery, that plaintiff be freed from the obligations thereof and permitting the plaintiff to marry again but forbidding the defendant to marry any person other than the plaintiff during the lifetime of the plaintiff except by express permission of the Court;

Ordered, adjudged, and decreed that the agreement, Exhibit 3, dated June 4, 1929, providing for the custody of the minor children, Craig Leonard and Stephanie Leonard, issue of said marriage, as well as providing for the support and maintenance of the plaintiff, be and hereby is approved and affirmed and made a part of the judgment herein, and as provided in said agreement, Exhibit 3, dated June 4, 1929, it is

Ordered, adjudged, and decreed that the plaintiff herein, Adelaide S. Leonard, have the sole care, custody, and control of the infant children, Craig Leonard and Stephanie Leonard, and that the defendant herein, Stephen J. Leonard, pay to the plaintiff herein, Adelaide S. Leonard, for and during the term of her natural life the sum of thirty-five thousand dollars ($35,000) per year;

Ordered, adjudged, and decreed that this judgment is interlocutory but shall become the final judgment as of course

101 three months after the entry and filing hereof unless for sufficient cause the court in the meantime shall have otherwise ordered. Upon this judgment becoming final, said marriage shall be dissolved and the plaintiff shall thereby be divorced from the defendant and it shall be lawful for the plaintiff to marry again the same as if the defendant were dead but it shall not be lawful for the defendant to marry any person other than the plaintiff during the lifetime of the plaintiff except by express permission of the Court.

W. T. C.

THOMAS M. FARLEY, *Clerk.* J. S. C.

CERTIFICATE OF COUNTY CLERK

I hereby certify that a decision of interlocutory judgment of divorce in favor of the plaintiff in an action brought in the Supreme Court by Adelaide S. Leonard, plaintiff, against Stephen J. Leonard, defendant, was entered in this office on the 22nd day of July 1929 and that no order has been filed in this action since the entry of interlocutory judgment.

Dated New York, N. Y., October 22, 1929.

THOMAS M. FARLEY,
Clerk of the County of New York.

No. 53040.

102 STATE OF NEW YORK,
County of New York, ss:

I, Thomas M. Farley, Clerk of the said County and Clerk of the Supreme Court of said State for said County, do certify that I have compared the preceding with the original final Judgment Leonard vs. Leonard cert. signed Oct. 22, 1929, on file in my office, and that the same is a correct Transcript therefrom, and of the whole of such original.

Indorsed Filed. July 22, 1929.

In witness whereof, I have hereunto subscribed my name and affixed my official seal, this 22 day of Oct. 1929.

THOMAS M. FARLEY, *Clerk.*

Please take notice that the within is a copy of the final judgment duly entered herein in the office of the Clerk of the within named Court in the Borough of Manhattan in the City of New York, on 22 day of October 1929.

Dated New York, Oct. 22, 1929.

JACKSON, FULLER, NASH & BROPHY,
Attorneys for Plaintiff.
Office and P. O. Address 15 Broad Street,
Borough of Manhattan, New York City.

To MARSHALL & AUCHINCLOSS, Esqs.,
Attorneys for defendant,
50 Broadway, N. Y.

103 File No. 21308. Year 1929. Supreme Court of the State of New York, County of New York. Adelaide S. Leonard, plaintiff, v. Stephen J. Leonard, defendant. Action for absolute divorce. Copy. Final Judgment, with notice of entry. Jackson, Fuller, Nash & Brophy, Attorneys for plaintiff, 15 Broad Street, Borough of Manhattan, New York City.

To MARSHALL & AUCHINCLOSS, Esqs.,
Attorneys for Defendant.

Due service of a copy of the within paper and notice of entry is hereby admitted this 23rd day of July 1929.

MARSHALL & AUCHINCLOSS,
Attorneys for Defendant.

104 *Exhibit 4, annexed to foregoing statement of evidence*

SUPPLEMENTAL AGREEMENT BETWEEN STEPHEN J. LEONARD, UNITED STATES TRUST COMPANY OF NEW YORK, AND ADELAIDE SHANAHAN LEONARD

Dated, ———.

Agreement made this 10th day of December 1929 between Stephen J. Leonard, now residing at Ritz Tower, Park Avenue and 57th Street, Borough of Manhattan, City, County, and State of New York, hereinafter called the Grantor, party of the first part, the United States Trust Company of New York, a corporation organized and existing under the laws of the State of New York, having its principal office and place of business at 45 Wall Street, Borough of Manhattan, City, County, and State of New York, hereinafter called the "Trustee", party of the second part, and Adelaide Shanahan Leonard, now residing at 420 Park Avenue, Borough of Manhattan, City, County, and State of New York, hereinafter referred to as the third party, party of the third part, witnesseth,

Whereas, under date of the 4th day of June 1929, the respective parties hereto executed a Trust Agreement which by one
105 of its terms permitted the amendment thereof by and with the consent of the Grantor and the Third Party, and

Whereas, the parties hereto desire to amend the terms of the said Agreement of the 4th day of June, 1929, in certain respects in regard to the deposit by the Grantor with the Trustee of shares of the capital stock of The Bankers Trust Company of New York,

Now, therefore, in consideration of the mutual covenants, hereinafter contained, the respective parties hereto agree as follows:

One. The time within which the Grantor shall withdraw the Eleven Hundred (1100) shares of the capital stock of The Bankers Trust Company of New York (hereinafter referred to as "Bankers Trust") from the trust fund created pursuant to the terms of the aforesaid agreement of June 4, 1929, is hereby

extended to and including the 10th day of January 1931, subject to the following terms and conditions:

(a) the Grantor at his option may at any time withdraw said shares or any part thereof from the trust fund upon his depositing with the Trustee in substitution therefor, either

(1) shares of the capital stock of The Equitable Trust Company of New York (hereinafter referred to as "Equitable Trust") having an aggregate market value equal to the aggregate market value of any shares of the Bankers Trust
106 withdrawn from said trust fund, provided that the number of shares of the Equitable Trust so deposited shall in no event exceed at any one time $74,800.00 in aggregate market value at the time of their deposit, or

(2) cash at the rate of $136.00 per share of the Bankers Trust withdrawn, provided that if the market value of any share of the Bankers Trust at the time of the withdrawal is in excess of $136.00 per share, the Grantor shall then pay to the Trustee the market value as determined by the Trustee to be thereafter accounted for in accordance with the terms of sub-paragraph (e) of this Section One.

(b) In the event that the Grantor shall desire to substitute any shares of the capital stock of Equitable Trust in place of shares of the capital stock of Bankers Trust, the Grantor or his duly authorized agent shall request in writing the Trustee to sell and the Trustee shall sell, pursuant to the directions of the Grantor as hereinafter mentioned, any shares of Bankers Trust, the proceeds of which are to be used for the purchase of shares of Equitable Trust; the value at which any said share of Equitable Trust shall be fixed for purposes of retention in the trust fund to be the value per share at which the same was purchased in the open market, or otherwise, plus all commissions paid. In the event that the proceeds from the sale of any
107 shares of the capital stock of Bankers Trust shall exceed the aggregate cost of shares of the capital stock of Equitable Trust, said excess proceeds shall be retained by the Trustee until January 10, 1931, or the date when all shares of the capital stock of Bankers Trust and Equitable Trust have been withdrawn from said trust fund by said Grantor or sold, as hereinafter mentioned, which ever date shall be the earlier.

(c) Anything in this supplemental agreement to the contrary notwithstanding, the Grantor shall have the right to require the Trustee to sell any shares of the capital stock of Bankers Trust at a price less than $136.00 for the purpose of immediately acquiring and substituting in the trust fund in place of the shares so sold, shares of the capital stock of Equitable Trust to the extent in this section mentioned.

(d) If at any time prior to January 10, 1931, the Grantor shall deem it advisable to sell any of the said shares of the capital stock of Bankers Trust and/or Equitable Trust, he shall forthwith write to the Trustee stating said fact, and the Trustee shall thereupon either sell said shares, or any part thereof, in the open market, or deliver said shares to or upon the order of the Grantor against payment therefor of the amount stated as the sales price by the Grantor in his letter directing delivery, provided that no sale of the capital stock of Bankers Trust may be made at
108 a price less than $136.00 per share (except for the purpose of an exchange of shares of the capital stock of Bankers Trust for shares of the capital stock of Equitable Trust, as hereinbefore mentioned), and no sale of shares of Equitable Trust may be made at a price less than the greater of either of the prices hereinafter mentioned in subdivisions (1) or (2) of this paragraph:-

(1) The price per share at which any shares of the capital stock of Equitable Trust were acquired in exchange for the capital stock of Bankers Trust at the time of their deposit in substitution therefor, or

(2) Such price per share as will realize to the trust fund an amount which when added to the net proceeds of any sales of shares of the capital stock of Bankers Trust and/or Equitable Trust then remaining on deposit in the trust fund, plus the then market value of any shares of Bankers Trust and Equitable Trust then remaining on deposit in the trust fund will equal the sum of $149,600.00.

Nothing hereinbefore set forth shall prevent the Grantor at his option, from selling any shares of the capital stock of Bankers Trust and/or Equitable Trust at prices less than hereinbefore stated, provided that at the time of such sale the Grantor shall pay into and deposit in the trust fund, as part thereof, the
109 difference between such price and the price per share necessary to protect said fund, so that at the time of said sale the aggregate market value of any shares of Bankers Trust and Equitable Trust then remaining on deposit in the trust fund, plus the proceeds of any shares then sold, shall equal the sum of $149,600.00. In his letter of authority to sell or deliver said shares for sale, the Grantor shall specify the sales price receivable (which shall be not less than the then market price as determined by the Trustee in its sole discretion, unless the Grantor shall at the time of said sale pay to the Trustee the difference between the then market price as so determined by the Trustee and the sales price specified by the Grantor), and until January 10, 1931, or such earlier time as all of said shares of the capital stock of Bankers Trust and Equitable Trust shall have been sold or with-

drawn from the said trust fund, whichever date shall be the earlier, the Trustee shall retain all of the proceeds of said sales.

(e) On January 10, 1931, or at the time when all of said shares of the capital stock of Bankers Trust and Equitable Trust shall have been withdrawn from said trust fund, whichever date is the earlier, an account shall be stated between the Trustee and the Grantor covering the sales of any shares of the capital stock of Bankers Trust and/or Equitable Trust made prior to said January 10, 1931, or the date of the withdrawal of all of said shares of bank stock, whichever date shall be the earlier.
110 Said account shall set forth the aggregate net profits, if any, receivable from all of said sales; net profits shall be determined by deducting from the aggregate proceeds (less commissions) of all sales of both Bankers Trust and Equitable Trust, the sum of $149,600.00 and any excess in amount over and above $149,600.00 then remaining in the possession of the Trustee is hereby agreed to be the net profits distributable, as hereinafter stated. Immediately upon the determination of the said aggregate net profits, if any, from all of said sales, the Trustee shall pay into the principal account of said trust fund one-third of said net profits, the balance of said net profits remaining in the possession of the Trustee to be thereupon paid to the Grantor.

Two. From and after January 1, 1930, and until January 10, 1931, or the date when all shares of the capital stock of Bankers Trust and Equitable Trust have been withdrawn from said trust fund by said Grantor, or sold, whichever date shall be the earlier, the Grantor shall pay into the trust fund, as income to the fund, interest at the rate of 6% per annum on $149,600.00 to be calculated and paid quarterly, the first payment to be made April 1, 1930; from which quarterly payments the Grantor shall credit himself and deduct the amount of any dividends which may be paid on and after January 1, 1930, to the Trustee by the Grantor by Bankers Trust and/or Equitable Trust upon any shares of said Trust Companies deposited in said trust fund. Any shares of the capital stock of either of said Trust Companies
111 received by the Trustee from stock dividends or split-ups, or the proceeds thereof, if sold, shall be retained by the Trustee until January 10, 1931, or until such time as all shares of the capital stock of both Trust Companies are withdrawn from the said trust fund, as herein provided for.

Three. (a) If on or before January 10, 1931, all of the aforesaid shares of the capital stock of Bankers Trust and Equitable Trust shall not have been sold, the Grantor shall on said date withdraw any shares of the capital stock of both of the aforesaid Trust Companies then remaining on deposit with the said Trustee and pay to the said Trustee at the time of said withdrawal;

(1) for each share of the capital stock of Bankers Trust so withdrawn the sum of $136.00 per share;

(2) for each share of the capital stock of Equitable Trust so withdrawn the greater of either of the prices mentioned in subdivisions (1) or (2) of subparagraph (d) of Section One of this Agreement.

(b) In addition on January 10, 1931, any shares of the capital stock of Bankers Trust and/or shares of the capital stock of Equitable Trust then remaining on deposit in the trust fund shall be valued by the Trustee as of January 10, 1931, at the closing bid price for said shares on said date. If the value of said shares as fixed by the Trustee, as aforesaid, shall be in excess of—

112 (1) $136.00 per share for each share of the capital stock of Bankers Trust then remaining on deposit and/or

(2) for each share of the capital stock of Equitable Trust then remaining on deposit a value per share in excess of the greater of either of the prices mentioned in subdivisions (1) or (2) of subparagraph (d) of Section One of this Agreement, the Grantor shall pay to the Trustee for deposit in the principal account of the trust fund on January 10, 1931, in addition to the amount mentioned in subdivision (a) of this Section Three, a sum equal to one-third of the difference between

(i) the value as fixed by the Trustee, as aforesaid, of said shares of Bankers Trust and/or Equitable Trust, and

(ii) the aggregate of the amounts mentioned in subdivision (a) of this Section Three.

(c) In the event that on January 10, 1931, the Grantor has not so withdrawn said shares of Bankers Trust and Equitable Trust and the trust fund has not realized at least the sum of $149,600.00 in cash in lieu thereof, the Trustee shall sell said shares at private or public sale without the necessity of giving the Grantor any notice whatsoever of the sale or the time or place thereof, and from the proceeds of the sale thereof and

113 the proceeds of any sales theretofore made, deposit such amount in the trust fund as shall equal—

(1) the sum of $149,600.00 plus interest thereon, if any, be then due, from January 1, 1930, to January 10, 1931, and

(2) one-third of any amount in excess of $149,600.00 then in the possession of the Trustee from the proceeds of any sales or any payments made by the Grantor against the withdrawal of any said shares; two-thirds of any excess over and above said $149,600.00 less all costs of the sale to be paid to the Grantor.

The Trustee shall not be liable to the Grantor, nor to any beneficiary of the Trust Agreement, for any deficiency in the event that the net proceeds of the aforesaid sale by the Trustee

do not amount to $149,600.00, plus interest thereon, if any, from January 1, 1930 to January 10, 1931, but nothing herein contained shall prevent any beneficiary from bringing any action against the Grantor to require the Grantor to pay into the trust fund the amount of any such deficiency. The Grantor covenants and agrees to pay to the Trustee any such deficiency which may be fixed by said Trustee at the time of the calculation thereof.

Four. Each and every other term of the Agreement dated the 4th day of June 1929 between the respective parties hereto is hereby ratified and confirmed in all respects.

114 In witness herfieof, the Grantor has hereunto set his hand and seal, the third party has hereunto set her hand and seal and the Trustee has caused its corporate seal to be hereunto affixed and these presents to be signed by one of its Vice Presidents and attested by its Secretary or one of its Assistant Secretaries, the day and year first above written.

STEPHEN J. LEONARD,
[L. S.] By BAYARD H. FAULKNER, *Attorney.*
UNITED STATES TRUST COMPANY OF NEW YORK,
Trustee,
By WILLIAMSON PELL, *First Vice President.*
Attest:
G. I. MANSELL, *Assistant Secretary.*
[L. S.] ADELAIDE SHANAHAN LEONARD,
Third Party.

Sept. 23/31, CRAIGH LEONARD.
In presence of—
JOHN G. JACKSON.

115 STATE OF NEW YORK,
County of New York, ss:-

On this 21st day of January, in the year 1930, before me personally came Bayard H. Faulkner as attorney for Stephen J. Leonard, to me personally known, and known to me to be one of the individuals described in, and who executed the within instrument, and acknowledged that he executed the same.

DONALD C. HOWE.
Donald C. Howe,
510 Park Avenue,
Notary Public, Westchester County.

Certificate filed in New York County. New York County Clerk's No. 551. New York Co. Register's No. 1-H-393. Commission Expires March 30, 1931.

116 STATE OF NEW YORK,
County of New York, ss:

On this 15 day of January, in the year 1930, before me came Williamson Pell, to me known, who being by me duly sworn, did depose and say that he resides in Rye, New York; that he is the First Vice President of United States Trust Company of New York, the corporation described in and which executed the above instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by order of the board of Trustees of said corporation, and that he signed his name thereto by like order.

(Signed) N. A. MULLINS,
N. A. Mullins,
Notary Public, Kings County, No. 744.

Cert. filed in New York Co. No. 743. New York Co. Reg. No. 1-M-496. Kings Co. Reg. No. 1389. Commission Expires Mch. 30, 1931.

117 STATE OF NEW YORK,
County of New York, ss:

On this 21st day of January, in the year 1930, before me personally came Adelaide Shanahan Leonard, to me personally known, and known to me to be one of the individuals described in, and who executed the within instrument, and acknowledged that she executed the same.

(Signed) DONALD C. HOWE,
Donald C. Howe,
510 Park Avenue,
Notary Public, Westchester County.

Certificate filed in New York County. New York County Clerk's No. 551. New York Co. Register's No. 1H-391. Commission Expires March 30, 1931.

118 *Exhibit 5, annexed to foregoing statement of evidence*

SUPPLEMENTAL AGREEMENT between STEPHEN J. LEONARD, UNITED STATES TRUST COMPANY OF NEW YORK, and ADELAIDE SHANAHAN LEONARD

November 17, 1930

Supplemental Agreement made this 17th day of November 1930, between Stephen J. Leonard, now residing at Ritz Tower, Park Avenue and 57th Street, Borough of Manhattan, City, County, and State of New York, hereinafter called the Grantor,

party of the first part, United States Trust Company of New York, a corporation organized and existing under the laws of the State of New York, having its principal office and place of business at 45 Wall Street, Borough of Manhattan, City, County, and State of New York, hereinafter called the "Trustee," party of the second part, and Adelaide Shanahan Leonard, now residing at 420 Park Avenue, Borough of Manhattan, City, County, and State of New York, hereinafter referred to as the third party, party of the third part, witnesseth,

Whereas, under date of the 10th of December 1929, an amendment to the original Trust Agreement, dated the 4th day of June 1929, between the Grantor, the Trustee, and the third
119 party, was executed providing for the extension of time during which the Grantor was required to dispose of or withdraw from the Trust Fund the 1,100 Shares of the Capital Stock of the Bankers Trust Company of New York now in the Trust Fund, and setting forth the rights and obligations in connection therewith of the respective parties, and

Whereas, the third party has now deemed it advisable to permit the Grantor to withdraw the aforesaid 1,100 Shares of the Capital Stock of the Bankers Trust Company of New York from said Trust Fund and has also agreed to waive her rights under the aforesaid amendment of the 10th day of December 1929, to any profit which she might have been entitled to upon the withdrawal or disposition of any of said shares prior to January 10, 1931, and

Whereas, the parties hereto desire to amend the terms of the aforesaid agreements dated the 4th day of June 1929 and the 10th day of December 1929 on the terms hereinafter stated,

Now, therefore, in consideration of the mutual covenants herein contained, the respective parties hereto agree as follows:

(1) Simultaneously with the execution and delivery of this agreement, the Grantor shall deliver to the Trustee to be deposited in the Trust Fund as part of the capital thereof, $149,500 prin-
cipal amount of McCulloch Oil Company Three Year 6%
120 First Mortgage Bonds, with coupon due March 1, 1931, and subsequent coupons attached together with cash or check for $100.00 to the order of the Trustee to be deposited in the principal account of the Trust Fund, and the third party hereby accepts said deposit of said Bonds and said $100.00 cash or check subject to collection in lieu of cash to the aggregate amount of $149,600.00 as full and complete satisfaction of the Grantor's obligations under the provisions of the aforesaid agreement of the 4th day of June, 1929, as amended by the supplemental agreement of the 10th day of December 1929, to complete the deposit with the Trustee of the entire principal amount of

the Trust Fund aggregating $650,000.00, provided that due payment of the aforesaid $149,500.00 principal amount of the aforesaid McCulloch Oil Company Bonds and the due payment of the interest thereon at the times and in the manner set forth in said Bonds, and the coupons attached thereto which is hereby guaranteed by the Grantor is actually made, and provided further that in accordance with Article 2 of the Original Trust Agreement dated the 4th day of June, 1929, the third party shall have the same rights with respect to the investment of the proceeds upon redemption or sale of the principal amount of the aforesaid McCulloch Oil Company Bonds as are granted to her by the aforesaid Article 2 of the original Trust Indenture.

(2) Simultaneously with the execution and delivery of
121 this agreement the Grantor shall pay to the Trustee in cash or check subject to collection the sum of $672.29 to be deposited in the income account of the Trust Fund in full and complete satisfaction of the obligations of the Grantor to pay to the Trustee the difference between the amount of dividends collected by the Trustee on the 1,100 Shares of the Capital Stock of the Bankers Trust Company of New York heretofore deposited in the principal account of the Trust Fund and the obligation of the Grantor to pay 6% on the sum of $149,600.00 from the date of the deposit of said shares of the Bankers Trust Company of New York in said Trust Fund to the date of execution and delivery of this supplemental agreement, less interest from September 1, 1930, to the date of the execution and delivery of this supplemental agreement, at 6% on the $149,500 principal amount of McCulloch Oil Company Bonds, with coupons annexed, to be deposited in the principal account of the Trust Fund as in this agreement provided for.

(3) Simultaneously with the execution and delivery of this agreement and upon delivery to the Trustee of the aforesaid $149,500.00 principal amount of McCulloch Oil Company, Three-Year 6% First Mortgage Bonds and the aforesaid checks for $100.00 and $672.29, the Trustee shall deliver to or upon the order of the Grantor the 1,100 Shares of the Capital Stock of the Bankers Trust Company of New York heretofore deposited in the principal account of the Trust Fund.

122 Each and every term of the original Trust Indenture dated the 4th day of June 1929, as amended by supplemental agreement dated the 10th day of December 1929, other than as herein amended is hereby ratified, confirmed, and approved in all respects and is to remain in full force and effect.

In witness whereof, the Grantor has hereunto set his hand and seal, the third party has hereunto set her hand and seal and the Trustee has caused its corporate seal to be hereunto affixed and

these presents to be signed by one of its Vice Presidents and attested by its Secretary or one of its Assistant Secretaries, the day and year first above written.

[L. S.] STEPHEN J. LEONARD, *Grantor.*

UNITED STATES TRUST COMPANY OF NEW YORK.
Trustee.

By T. H. WILSON, *Vice President.*

Attest:

J. MANSELL.
Assistant Secretary.

[L. S.] ADELAIDE S. LEONARD,
Third Party.

Sept. 23/31, CRAIGH LEONARD.
In presence of—
JOHN E. JACKSON.
Executed in Triplicate No. 1.

123 STATE OF NEW YORK,
County of New York, ss:

On this 17th day of November, in the year 1930, before me personally came Stephen J. Leonard, to me personally known, and known to me to be one of the individuals described in, and who executed the within instrument, and acknowledged that he executed the same.

JOHN F. CLANCY.
Notary Public.

New York Co. Clerk's No. 95. New York Co. Register's No. 1C307. Term Expires March 30, 1931.

124 STATE OF NEW YORK.
County of New York, ss:

On this 18th day of November, in the year 1930, before me came Thomas H. Wilson, to me known, who, being by me duly sworn, did depose and say that he resides in Scarsdale, N. Y.; that he is the Vice President of United States Trust Company of New York, the corporation described in and which executed the above instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by order of the board of Trustees of said corporation, and that he signed his name thereto by like order.

CHARLES S. YARWOOD, JR.,
Charles S. Yarwood, Jr.,
Notary Public.

Queens Co. Clk's No. 1993. Reg. No. 6578. Cert. filed in N. Y. Co. Clk's No. 17, Reg. No. 1-Y-16. Commission expires March 30th, 1931.

125 STATE OF NEW YORK,
County of New York, ss:

On this 3rd day of November, in the year 1930, before me personally came Adelaide Shanahan Leonard, to me personally known, and known to me to be one of the individuals described in, and who executed the within instrument, and acknowledged that she executed the same.

[Name illegible],
Notary Public, Kings Co.

Certificate Filed in N. Y. Co. 354. Commission Expires Mar. 30, 1932.

126 MARSHALL & AUCHINCLOSS,
50 BROADWAY, NEW YORK,
November 24, 1930.

Snowden Marshall, Gordon Auchincloss, Donald Duncan. Telephone Digby 7020. Cable Address, Parkmarsh.

UNITED STATES TRUST COMPANY OF NEW YORK,
45 Wall Street, New York City.

GENTLEMEN: In the second Supplemental Agreement to the Trust Agreement of June 4, 1929, between your institution, Stephen J. Leonard, and Adelaide Shanahan Leonard, reference is made to the original Agreement of June 4th and the first Supplemental Agreement dated December 10, 1929.

Through typographical errors on Page 1, Page 2, and Page 5, of the second Supplemental Agreement, dated November 17, 1930, just recently executed, the first Supplemental Agreement of December 10, 1929, is referred to as the 10th of February 1929.

Will you kindly change in the original Agreement the dates of the 10th of February 1929, to the 10th of December 1929 to reflect the true intent of the Agreement.

Yours very truly,

J. DONALD DUNCAN.

127 To the UNITED STATES TRUST COMPANY,
45 Wall Street, New York City.

We have examined the Supplemental Agreement of November 17, 1930, between us and you and understand that the 10th of February 1929 was inadvertently written in three places, instead of the 10th of December 1929.

We, accordingly, hereby consent to your changing the original agreement which we have executed in that respect and authorize

you on our behalf to elide the words 10th of February 1929, and insert in place thereof the 10th of December 1929.

STEPHEN J. LEONARD.
ADELAIDE S. LEONARD.

JDD/msm.

128 *Exhibit 6, annexed to foregoing statement of evidence*

SUPPLEMENTAL AGREEMENT BETWEEN STEPHEN J. LEONARD, UNITED STATES TRUST COMPANY OF NEW YORK, AND CRAIGH LEONARD, TRUSTEE, AND ADELAIDE SHANAHAN LEONARD, DATED JUNE 23, 1932.

Supplemental Agreement made as of the 23rd day of June, 1932, between Stephen J. Leonard, now residing at 1067 Fifth Avenue, Borough of Manhattan, City, County, and State of New York, hereinafter called the "Grantor," party of the first part, United States Trust Company of New York, a corporation organized and existing under the laws of the State of New York, having its principal office and place of business at 45 Wall Street, Borough of Manhattan, City, County, and State of New York, and Craigh Leonard, of the Borough of Manhattan, City and State of New York, hereinafter jointly called the "Trustee," party of the second part, and Adelaide Shanahan Leonard, now residing at 770 Park Avenue, Borough of Manhattan, City, County, and State of New York, hereinafter referred to as the "Third Party," party of the third part, witnesseth,

129 Whereas, under date of the 4th day of June 1929, an original trust agreement was executed between the Grantor, the Trustee and the Third Party which was subsequently amended by supplemental agreements under date of the 10th day of December 1929 and the 17th day of November 1930, and

Whereas, the parties hereto desire to amend the terms of the aforesaid agreements dated the 4th day of June 1929; the 10th day of December 1929, and the 17th day of November 1930, on the terms hereinafter stated.

Now, therefore, in consideration of the mutual convenants herein contained, the respective parties hereto agree as follows:

(1) Simultaneously with the execution and delivery of this supplemental agreement, the Grantor shall deliver to the Trustee to be deposited in the Trust Fund as part of the capital thereof Ten Thousand Dollars ($10,000.00) principal amount of McCulloch Oil Company Three Year 6% First Mortgage Bonds, due March 1, 1932, without any coupons attached, and the Trustee hereby accepts said deposit subject to the terms and conditions hereinafter stated.

(2) The Third Party hereby authorizes and directs the Trustee:

(a) To deliver to the Grantor at the time of the delivery to said Trustee of this executed supplemental agreement the bonds listed in Schedule A annexed hereto and made a part hereof which the Grantor hereby agrees to accept as the equivalent and market value of Ten Thousand Dollars ($10,000.00), and as the purchase price of the aforesaid McCulloch Oil Company bonds mentioned in paragraph (1) hereof.

(b) To execute and deliver such documents as may be necessary in the opinion of the law firm of Auchincloss & Duncan, of 50 Broadway, Borough of Manhattan, City and State of New York, as attorneys for the Grantor, and the law firm of Jackson Euller Nash & Brophy, of 15 Broad Street, Borough of Manhattan, City and State of New York, as attorneys for the Third Party, to carry out the proposed reorganization of the Oklahoma Company (a Delaware Corporation), and without limiting the generality of such power specifically

(i) to execute the acceptance of the proposal of Edgar T. Noble, of the City of Okmulgee, State of Oklahoma, when delivered to the Trustee with the executed acceptance of all other bondholders of the present outstanding issue (aggregating $556,500.00 in principal amount) of McCulloch Oil Company Three-Year 6% First Mortgage Bonds, providing for the organization of a new company (hereinafter referred to as the "New Corporation"), to take over the properties and assets of the aforesaid Oklahoma Company, and to have said New Corporation execute and issue new First Mortgage Bonds to be exchanged for the present issue of McCulloch Oil Company Three Year 6% First Mortgage Sinking Fund Gold Bonds, and

(ii) To exchange the Two Hundred and Eight Thousand Five Hundred Dollars ($208,500.00) principal amount of McCulloch Oil Company Three Year 6% First Mortgage Sinking Fund Gold Bonds now in the Trust Fund for a like principal amount of First Mortgage Bonds of the New Corporation, and

(iii) to exchange the Ten Thousand Dollars ($10,000.00) principal amount of McCulloch Oil Company Bonds mentioned in paragraph (1) hereof and the Fifteen Thousand Dollars ($15,000.00) principal amount of McCulloch Oil Company Bonds mentioned in subdivision (c) of this paragraph (2) if said Bonds are deposited in the Trust Fund, for a like principal amount of First Mortgage Bonds of the New Corporation, and

(iv) to exchange the Ten Thousand Dollars ($10,000.00) principal amount of Escrowed Security Bonds and the Fifteen Thousand Dollars ($15,000.00) principal amount of Additional Escrowed Security Bonds if deposited in the form

of McCulloch Oil Company Bonds, hereinafter mentioned in paragraph (3) hereof, for a like principal amount of First Mortgage Bonds of the New Corporation, and

(v) in order to facilitate the purchase (by the holders of the present McCulloch Oil Company Three Year 6% First Mortgage Sinking Fund Gold Bonds) of the properties and assets of the Oklahoma Company at receivership or foreclosure sale, or otherwise, as aforesaid counsel for the Grantor and the Third Party may advise, to send any principal amount of McCulloch Oil Company Three Year 6% First Mortgage Sinking Fund Gold Bonds now or hereafter deposited in the Trust Fund, to a correspondent bank in the City of Tulsa, Oklahoma, in order that any bid of the bondholders at said sale may be endorsed on said Bonds by the Court or the Receiver, as the case may be, as a credit thereon pending the exchange of said Bonds for the Bonds of the New Corporation.

(c) To execute and deliver to Edgar T. Noble of the City of Okmulgee, State of Oklahoma, or such corporation as he may nominate and designate in writing to the Trustee, a written option of purchase in such form as may be satisfactory to the aforesaid law firms of Auchincloss & Duncan and Jackson
133 Fuller Nash & Brophy, entitling the said Edgar T. Noble, or his said assignee, to purchase from the Trust Fund at any time within sixty (60) days from the date when the aforesaid New Corporation, mentioned in subsection (i) of subdivision (b) of this paragraph, shall have acquired legal and valid title to the properties and assets of the Oklahoma Company (an Oklahoma Corporation) pursuant to the terms of sale of said properties and assets which are now in receivership in the District Court of Tulsa County, Oklahoma (such date of acquisition of said properties by said New Corporation to be certified to the Trustee in writing by the said law firm of Auchincloss & Duncan, and in any event to be not later than the 20th day of September, 1932), One Hundred Thousand Dollars ($100,000.00), or any part thereof, in principal amount of such First Mortgage Bonds of the New Corporation which shall have been received by the Trustee in exchange for a like principal amount of Three Year 6% First Mortgage Bonds of the McCulloch Oil Company now owned by said Trustee, for the purchase price of Fifty Thousand Dollars ($50,000.00) plus accrued interest from March 1, 1932, at the rate of six per cent (6%) per annum on the principal amount of Bonds purchased.

(d) At any time while and if the Trustee shall hold, pursuant to the terms of this Indenture as amended, Ten Thousand
134 Dollars ($10,000.00) (or any part thereof) principal amount of First Mortgage Bonds of the New Corporation,

the Grantor is hereby given the right to repurchase said Ten Thousand Dollars ($10,000.00) (or such actual amount less thereof as may then be held by said Trustee) principal amount of said First Mortgage Bonds of said New Corporation for the sum or purchase price of One Thousand Dollars ($1,000.00) per One Thousand Dollars ($1,000.00) principal amount of Bonds purchased, plus accrued interest, if any, to the date of purchase at the coupon rate mentioned in the coupons attached to said Bonds, except that, if at any time while the Trustee shall so hold any of said Ten Thousand Dollars ($10,000.00) principal amount of said Bonds, it shall receive from anyone other than the Grantor a bid to purchase said Bonds (or any part thereof) at a price satisfactory to the Trustee, and the Trustee desires to accept said bid, it may sell said Bonds (or any part thereof) to said bidder, provided only, that it has notified the Grantor in writing or by telegram or cable of the terms of said bid and given the Grantor the same opportunity to purchase the said Bonds (or any part thereof), on the exact terms mentioned in said bid. If the Trustee shall sell to Edgar T. Noble, or his nominee, said One Hundred Thousand Dollars principal amount of Bonds mentioned in subdivision (c) of this paragraph (2), it is understood
135 that such sale shall not be construed to include the Ten Thousand Dollars ($10,000.00) principal amount of Bonds referred to in this subdivision (d) of this paragraph (2), but nothing in this subdivision contained shall be deemed to prevent the Trustee from making an immediate sale of said Bonds to any bidder other than the Grantor if the terms of such bid require an immediate acceptance.

(e) At any time during the lifetime of the Third Party and upon receipt by the Trustee of a letter from the Third Party consenting thereto, to deliver to the Grantor such additional Bonds or other Securities, selected by the Grantor, then comprised within the investments of the Trust Fund (other than McCulloch Oil Company Three Year 6% First Mortgage Bonds due March 1, 1932, or any Bonds of the aforesaid New Corporation issued in exchange therefor) having a then market principal value of Fifteen Thousand Dollars ($15,000.00) upon tender to the Trustee by the Grantor in payment therefor of Fifteen Thousand Dollars ($15,000.00) principal amount of either McCulloch Oil Company Three Year 6% First Mortgage Bonds due March 1, 1932, or Fifteen Thousand Dollars ($15,000.00) principal amount of First Mortgage Bonds of the aforesaid New Corporation, and upon tender by the said Grantor of the Additional Escrowed Security Bonds referred to in paragraph (4) of this Agreement.

136 (f) At any time while and if the Trustee shall hold, pursuant to the terms of this Indenture as amended the Fifteen Thousand Dollars ($15,000.00) (or any part thereof), principal amount of McCulloch Oil Company First Mortgage Bonds or First Mortgage Bonds of the New Corporation exchanged therefor and which may have been deposited in the Trust Fund by the Grantor pursuant to the terms of subdivision (e) of this paragraph (2), the Grantor is hereby given the right to repurchase said Fifteen Thousand Dollars ($15,000.00) (or such actual amount less thereof as may then be held by said Trustee), principal amount of said First Mortgage Bonds for the sum or purchase price of Fifteen Thousand Dollars ($15,000.00) plus accrued interest, if any, to the date of purchase at the coupon rate mentioned in the coupons attached to said Bonds, except that if at any time while the Trustee shall so hold any of said Fifteen Thousand Dollars ($15,000.00) principal amount of said Bonds, it shall receive from anyone other than the Grantor a bid to purchase said Bonds (or any part thereof) at a price satisfactory to the Trustee, and the Trustee desires to accept said bid, it may sell said Bonds (or any part thereof) to said bidder, provided only, that it has notified the Grantor in writing or by telegram or cable of the terms of said bid and given the Grantor the same opportunity to purchase the
137 said Bonds (or any part thereof) on the exact terms mentioned in said bid. If the Trustee shall sell to Edgar T. Noble, or his nominee, said One Hundred Thousand Dollars principal amount of Bonds mentioned in subdivision (c) of this paragraph (2), it is understood that such sale shall not be construed to include the Fifteen Thousand Dollars ($15,000.00) principal amount of Bonds referred to in this subdivision (f) of this paragraph (2), but nothing in this subdivision contained shall be deemed to prevent the Trustee from making an immediate sale of said Bonds to any bidder other than the Grantor if the terms of such bid require an immediate acceptance.

(3) As security for the payment of the principal and interest when due of the Ten Thousand Dollars ($10,000.00) principal amount of McCulloch Oil Company Bonds (or the Ten Thousand Dollars ($10,000.00) principal amount of First Mortgage Bonds of the New Corporation to be issued in exchange therefor), mentioned in paragraph (1) and subdivision (b) of paragraph (2) hereof, the Grantor hereby deposits with the Trustee in escrow but not as part of the Trust Fund, an additional Ten Thousand Dollars ($10,000.00) principal amount of McCulloch Oil Company Three Year 6% First Mortgage Bonds due March 1, 1932, without any coupons attached (hereinafter referred to as the "Escrowed Security Bonds"), and hereby authorizes the Trustee

to hold said Escrowed Security Bonds, or the First
138 Mortgage Bonds of the New Corporation when issued in exchange therefor pursuant to subsection (iv) of subdivision (b) of paragraph (2) hereof until such time

(a) as the Grantor may have exercised the right of repurchase of said Ten Thousand Dollars ($10,000.00) principal amount of Bonds granted to him pursuant to the terms of subdivision (d), of paragraph (2) hereof, or

(b) as the Trustee may have sold the said Ten Thousand Dollars ($10,000.00) principal amount of Bonds referred to in (a) of this paragraph, or

(c) as the New Corporation may have paid or redeemed such of the Bonds exchanged for the said Ten Thousand Dollars ($10,000.00) principal amount of Bonds mentioned in paragraph (1) hereof as the Trustee has not sold, and

at either of the times mentioned in subdivisions (a) and (c) of this paragraph (3) and upon the happening of the event therein described, the Trustee shall redeliver to the Grantor the said Escrowed Security Bonds free and clear of any lien whatsoever. If the Trustee shall have sold to any purchaser other than the Grantor the Ten Thousand Dollars ($10,000.00) principal amount of Bonds (or any part thereof) referred to in subdivision
139 (a) of this paragraph at a price less than the principal amount thereof and all accrued interest, the Trustee is hereby authorized to sell such amount of the Escrowed Security Bonds as may be necessary to make up the difference between the aforesaid sales price and the principal amount and accrued interest of Bonds sold by it, and the proceeds from such sale of such Escrowed Security Bonds to the extent necessary to make such deficit good, shall be paid over and into the Trust Fund as part thereof. Any excess of the proceeds from the sale of such Escrowed Security Bonds over and above the amount necessary to be paid into the Trust Fund as aforesaid and any Escrowed Security Bonds not sold by the Trustee, shall be returned to the Grantor with all unmatured coupons attached. During the entire time of the escrow of said Escrowed Security Bonds so long as the New Corporation shall not be in default in the payment of the interest or principal of the Ten Thousand Dollars ($10,000.00) principal amount of Bonds of the New Corporation exchanged for the Bonds mentioned in paragraph (1) hereof, the Trustee as Escrow Depositary shall clip each and every respective coupon from the said Escrowed Security Bonds when and as due and payable and deliver them forthwith to the Grantor for collection as his individual property.

(4) If at any time the Grantor shall exercise the rights granted him in subdivision (e) of paragraph (2) of this Agreement, as

security for the payment of the principal and interest when
140 due of the Fifteen Thousand Dollars ($15,000.00) principal amount of McCulloch Oil Company Bonds, (or the Fifteen Thousand Dollars ($15,000.00) principal amount of First Mortgage Bonds of the New Corporation when exchanges therefor), mentioned in subdivision (e) of paragraph (2) of this Agreement, the Grantor shall deposit with the Trustee in escrow but not as part of the Trust Fund an additional Fifteen Thousand Dollars ($15,000.00) principal amount of McCulloch Oil Company Three Year 6% First Mortgage Bonds due March 1, 1932, without any coupons attached, or Fifteen Thousand Dollars ($15,000.00) principal amount of First Mortgage Bonds of the New Corporation which may have then been exchanged therefor (hereinafter referred to as the "Additional Escrowed Security Bonds"), and the Trustee is hereby authorized to hold said Additional Escrowed Security Bonds when delivered to it as aforesaid until such time

(a) as the Grantor may have exercised the right of repurchase of the Fifteen Thousand Dollars ($15,000.00) principal amount of Bonds granted to him pursuant to the terms of subdivision (f) of paragraph (2) hereof, or

(b) as the Trustee may have sold the said Fifteen Thousand Dollars ($15,000.00) principal amount of Bonds referred to in (a) of this paragraph, or

(c) as the New Corporation may have paid or redeemed
141 the bonds exchange for the said Fifteen Thousand Dollars ($15,000.00) principal amount of Bonds mentioned in subdivision (e) of paragraph (2) hereof, and

at either of the times mentioned in subdivisions (a) and (c) of this paragraph (4) and upon the happening of the event therein described, the Trustee shall redeliver to the Grantor the said Additional Escrowed Security Bonds free and clear of any lien whatsoever. If the Trustee shall have sold to any purchaser other than the Grantor the Fifteen Thousand Dollars ($15,000.00) principal amount of Bonds (or any part thereof) referred to in subdivision (a) of this paragraph at a price less than the principal amount thereof and all accrued interest, the Trustee is hereby authorized to sell such amount of the Additional Escrowed Security Bonds as may be necessary to make up the difference between the aforesaid sales price and the principal amount and accrued interest of Bonds sold by it, and the proceeds from such sale of such Additional Escrowed Security Bonds to the extent necessary to make such deficit good, shall be paid over and into the Trust Fund as part thereof. Any excess of the proceeds from the sale of such Additional Escrowed Security Bonds over and above the amount necessary to be paid into the Trust Fund as

aforesaid and any Additional Escrowed Security Bonds not sold by the Trustee, shall be returned to the Grantor with all unmatured coupons attached. During the entire time of the escrow of said Additional Escrowed Security Bonds so long as the New Corporation shall not be in default in the payment
142 of the interest or principal of any First Mortgage Bonds of said New Corporation deposited under the terms of this Agreement, the Trustee, as Escrow Depositary, shall clip each and every respective coupon from the said Additional Escrowed Security Bonds when and as due and payable and deliver them forthwith to the Grantor for collection as his individual property.

(5) If the Trustee shall sell any or all of the One Hundred Thousand Dollars ($100,000.00) principal amount of Bonds mentioned in subdivision (c) of paragraph (2) of this Agreement pursuant to the terms of the option therein granted to Edgar T. Noble, or such Corporation as he may nominate and designate, the Grantor is hereby released from the guarantee (heretofore given by him to Third Party) of the payment in full of the principal of such bonds as may be so sold by the Trustee at less than par.

(6) Nothing in this supplemental agreement set forth in regard to the options given to the Grantor or to Edgar T. Noble, or any corporation which he may designate, shall be construed to in any way interfere with the authority of the Trustee as such to deal or take any action with regard to such McCulloch Oil Company First Mortgage Bonds or the First Mortgage Bonds of the aforesaid New Corporation exchanged therefor which shall at any time be comprised within the Trust Fund as the Trustee may deem advisable in the event that there shall be any default
143 in the payment of principal or interest of said Bonds during the period of time comprised within such options.

(7) Each and every other term of the original trust agreement of June 4, 1929, and all supplemental indentures thereof are hereby ratified and confirmed to be in full force and effect, except as herein expressely modified.

In witness whereof, the Grantor has hereunto set his hand and seal, the Third Party has hereunto set her hand and seal and the Trustee has caused its corporate seal to be hereunto affixed and these presents to be signed by one of its Vice Presidents and

attested by its Secretary or one of its Assistant Secretaries the day and year first above written.

[L. S.] STEPHEN J. LEONARD, *Grantor.*
UNITED STATES TRUST COMPANY OF NEW YORK,
Trustee,
By W. PELL, *1st Vice President.*

Attest:
J. MANSELL, *Assistant Secretary*
CRAIGH LEONARD, *Trustee.*
[L. S.] ADELAIDE S. LEONARD, *Third Party.*

144 STATE OF NEW YORK,
County of New York, ss:

On this 23rd day of June, in the year 1930, before me personally came Stephen J. Leonard, to me personally known, and known to me to be one of the individuals described in, and who executed the within instrument, and acknowledged that he executed the same.

JOHN F. CLANCY,
Notary Public.

New York Co. Clerk's No. 95. New York Co. Register's No. 1C307. Term Expires March 30, 1931.

145 STATE OF NEW YORK,
County of New York, ss:

On this 24th day of June, in the year 1932, before me came Williamson Pell, to me known, who being by me duly sworn, did depose and say that he resides in Village of Rye, New York; that he is the 1st Vice President of United States Trust Company of New York, the corporation described in and which executed the above instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by order of the board of Trustees of said corporation, and that he signed his name thereto by like order.

N. A. MULLINS,
N. A. Mullins,
Notary Public, Kings County, No. 750.

Cert. filed in New York Co. No. M-737. New York Co. Reg. No. 3-M-486. Kings Co. Reg. No. 3840. Commission expires Mch. 30, 1933.

146 STATE OF NEW YORK,
County of New York, ss:

On this 23rd day of June, in the year 1932, before me personally came Adelaide Shanahan Leonard, to me personally known, and known to me to be one of the individuals described in, and who executed the within instrument, and acknowledged that she executed the same.

JOHN F. CLANCY,
Notary Public.

New York Co. Clerk's No. 95. New York Co. Register's No. 1C307. Term Expires March 30, 1931.

Exhibit A

$4,000.00 American Telephone & Telegraph Company Gold Debenture Bond, due February 1, 1965. Interest due in February and August, at 5%. Listed on New York Stock Exchange.

$7,000.00 Union Gulf Corporation Collateral Trust Sinking Fund Gold Bond, due July 1, 1950. Interest due in January and July at 5%. Listed on the Curb.

147 In United States Circuit Court of Appeals, for the Second Circuit

[Title omitted.]

Stipulation re consolidation, etc.

It is hereby stipulated and agreed by and between the attorney for the Commissioner and the attorney for the Taxpayer, subject to the approval of the United States Circuit Court of Appeals for the Second Circuit:

(1) That the above entitled appeals be consolidated and treated as a single appeal.

(2) That the joint statement of evidence and exhibits referred to therein heretofore filed with the United States Board of Tax Appeals is the statement of evidence of the Commissioner and the Taxpayer.

148 (3) That the joint praecipe heretofore filed with the United States Board of Tax Appeals is the praecipe of the Commissioner and the Taxpayer.

(4) That the transcript of record transmitted by the United States Board of Tax Appeals is the record of both the Commissioner and the Taxpayer and the same shall be printed as one document.

(5) That the cost of printing the consolidated transcript of record shall be taxed one-half to the Commissioner and one-half to the Taxpayer.

(6) That the Taxpayer have 30 days after the filing of the printed record to serve and file a brief as to all matters covered by the consolidated appeals, and that the Commissioner have 20 days thereafter to serve and file a brief as to all matters covered by the consolidated appeals and the Taxpayer have 10 days thereafter to serve and file a reply brief as to all matters covered by the consolidated appeals.

JAMES W. MORRIS,
Attorney for Commissioner.
J. DONALD DUNCAN,
Attorney for Taxpayer.

149 Before United States Board of Tax Appeals

[Title omitted.]

Praecipe for record

To the Clerk of the United States Board of Tax Appeals:

You are hereby requested to prepare and certify and transmit to the Clerk of the United States Circuit Court of Appeals for the Second Circuit, with reference to the petitions for review heretofore filed in the above cause, a transcript of the record in the above cause, prepared and transmitted as required by law and by the rules of said Court, and to include in said transcript of record the following documents or certified copies thereof, to wit:

(1) The docket entries of all proceedings before the Board of Tax Appeals.

(2) Pleadings before the Board of Tax Appeals, as follows:

150 (a) Petition for redetermination and exhibits.

(b) Answer of the respondent.

(3) The findings of fact and opinion of the Board of Tax Appeals.

(4) The decision of the Board.

(5) The petitions for review filed in the above cause.

(6) The statement of evidence with Exhibits 1, 2, 3, 4, 5, and 6 attached thereto.

(7) Stipulation for the record.

(8) This Praecipe.

J. P. WENCHEL,
Attorney for Commissioner.

(Sgd.) J. DONALD DUNCAN,
Attorney for Taxpayer.

151 [Clerk's certificate to foregoing transcript omitted in printing.]

152 In United States Circuit Court of Appeals for the Second Circuit

No. 34—October Term, 1938

Argued Feb. 8, 1939. Decided June 30, 1939

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

STEPHEN J. LEONARD, RESPONDENT

STEPHEN J. LEONARD, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appeal from the Board of Tax Appeals.

Before L. HAND, SWAN, and AUGUSTUS N. HAND, Circuit Judges.

On separate petitions by the Commissioner of Internal Revenue and the taxpayer, to review an order of the Board of Tax Appeals affirming in part and reversing in part, a deficiency assessed against the taxpayer for income taxes for the year 1929.

J. Donald Duncan, of New York City, for Leonard.

L. W. Post, Sp. Asst. to Atty. Gen., for Helvering, Commissioner.

Opinion

L. HAND, Circuit Judge: This case comes up upon appeals by the Commissioner and the taxpayer from an order of the Board of Tax Appeals, assessing a deficiency against the taxpayer for the year 1929. The facts are as follows: On December 27, 1928, the wife of Leonard, the taxpayer, who was already living apart from him, began a suit for divorce against him in New York. While this was pending, the spouses executed two instruments, a deed of trust and a separation agreement, both on June 4, 1929. The deed conveyed property worth about $650,000 to a trustee, which was to pay $5,000 annually to each of the couple's three children, and the remainder of the income to the wife: the other provisions of the deed are not relevant to this controversy. The separation agreement recited the deed and the expectation of both parties that the wife would receive an income of $15,000 from the trust, and an equal sum from earlier gifts, so that she would have an invested income of $30,

000 from all sources. To bring her total allowance for maintenance up to $65,000, Leonard promised to pay her $35,000 more, as a maximum, subject however to reduction to not less than $10,000, if he should later convince the divorce court that his means no longer justified any larger sum. In consideration of these provisions the wife agreed to assume all her living expenses, thus discharging the husband from his duty of support. The decree of divorce, which became absolute in October 22, 1929, incorporated the separation agreement, "approved and
153 affirmed" it, and directed Leonard to pay his wife $35,000 "during the term of her natural life." Between June 4th and December 31, 1929, the trustee received income of $16,191.34 from the trust property, of which it distributed $5,200 to the wife, and five-twelfths of $5,000—$2,083.33—to each of the three children, leaving an undistributed balance of income for that period of about $4,700. The Board assessed Leonard upon the income distributed to his wife and minor children on the theory that these payments were in discharge of his continuing marital and paternal duties, but refused to assess him upon the undistributed income. Both parties appealed.

So far as we have found, no case has ever arisen in which a husband has discharged his duty of maintenance by the payment of a lump sum, but we are confident that in such a case any income, derived by the wife from the money received, would be assessed against her, regardless of the fact that the payment had relieved the husband pro tanto. Her income would be altogether beyond his control, its increase or decrease would not affect him at all, and it could be regarded as still his only by the most patent fiction. We see no difference, when, instead of a lump sum, the husband creates a trust in discharge of his duty; and in the only two cases where that situation has come before the courts, the income has been held to be taxable to the wife. Commissioner v. Tuttle, 6 Cir., 89 F. 2d 112; Fitch v. Commisioner, 8 Cir., 103 F. 2d 702. On the other hand such trusts will be only security if the husband's duty continues after decree, because the law or the decree reserves power to the divorce court to change its original award. Douglas v. Willcuts, 296 U. S. 1, 56 S. Ct. 59, 80 L. Ed. 3, 101 A. L. R. 391, was such a case. The spouses lived in Minnesota, by whose law the divorce court, not only was not bound by any agreement between them, but—and this was the critical fact—might later change the original allowance, if circumstances made it desirable. That was true also of Helvering v. Coxey, 297 U. S. 694, 56 S. Ct. 498, 80 L. Ed. 986, where the spouses lived in New Jersey, in which a settlement, though made with the wife's concurrence, does not end the power of the divorce court. Greenberg v. Greenberg, 99 N. J. Eq. 461, 133 A. 768.

The question therefore is whether a decree in the state of the divorce terminates the husband's duty and substitutes finally the provisions which it incorporates. In New York §§ 1155 & 1170 of the Civil Practice Act do indeed give the divorce court power to change allowances fixed in the original decree; and § 51 of the Domestic Relations Law, Consol. Laws N. Y. c. 14, forbids a wife's making an agreement discharging her husband's duty to support her. Nevertheless, a settlement made in discharge of the husband's duty is finally binding upon the parties to the divorce, if incorporated into the decree; and its terms will not be changed, unless the wife can disaffirm it for fraud, overreaching, or the like. Galusha v. Galusha, 116 N. Y. 635, 22 N. E. 1114, 6 L. R. A. 487, 15 Am. St. Rep. 453; Id., 138 N. Y. 272, 33 N. E. 1062; Cain v. Cain, 188 App. Div. 780, 177 N. Y. S. 178; Hamlin v. Hamlin, 224 App. Div. 168, 230 N. Y. S. 51. Kunker v. Kunker, 230 App. Div. 641, 246 N. Y. S. 118, seems an exception to this doctrine, though it is not entirely clear on just what grounds the majority did proceed. If they meant to hold that the agreement, though unimpeached, is not conclusive, the decision seems to us at variance with the law as previously laid down.

In the case at bar, if the trust had been the only consideration for the discharge of Leonard's duty, the income would not, therefore, have been taxable to him: his liability would have ended with the decree, which the court could not have reopened, and the case would have fallen within Commissioner v. Tuttle, supra, and Fitch v. Commissioner, supra. The situation was not, however, quite as simple as that, for the settlement agreement added to the trust a promise to pay alimony which the court might change and fix between $10,000 and $35,000. The question therefore becomes whether this changed the trust into a partial security for a total allowance, made up of the present income of the trust and of so much as the court might from time to time allow, and whether this control over it brings the situation within Douglas v. Willcuts, supra. We think it did not. It seems to us that the intent was that Leonard should never be obliged to make good any deficits caused by decrease in the trust income, or to be relieved by its increase; the original income was taken as the equivalent of a maintenance of $15,000, and discharged his
154 pro tanto. That is the more natural view. Possibly, however, there may be an indirect relation between the trust income and the amount fixed in the future by the divorce court under the separation agreement. It is true that the agreement apparently makes the only test the husband's "circumstances and ability to pay," but that does not necessarily mean that nothing

else will be considered. It may be that the wife's other means will also be deemed a factor, and in this way the income of the trust indirectly will determine the allowance. But that circumstance alone is not enough to make that income taxable to him; for if it were, the income from the earlier gifts would be similarly taxable, because that, too, was a factor in the original settlement. Moreover, consistently we should have to go a step farther, for it is the commoner practice in fixing alimony to take into consideration the wife's independent income from all sources. Sullivan v. Sullivan, 170 Mich. 557, 136 N. W. 482; Dietrick v. Dietrick, 88 N. J. Eq. 560, 103 A. 242. Obviously it would be absurd to tax the husband upon all this income, and it follows that a more direct correspondence is necessary than anything arising from the power reserved in the decree, even if, as we are disposed not to believe, the income of the trust was not for all purposes to be deemed an equivalent of $15,000.

We conclude therefore that the Board was wrong in assessing the husband for that part of the income payable to the wife. In so holding, it seems to us that our decision in Helvering v. Brooks, 2 Cir., 82 F. 2d 173, must be overruled. There we held that the income from a trust made in settlement with a wife, who was suing for divorce, was taxable to the husband. It is said that by the law of Florida—the place of the divorce—the divorce court had power later to change the allowance, as fixed in the settlement, to correspond with changes in the husband's means; and perhaps that was so. But we had nothing of the sort in mind, and the decision stands for more. Douglas v. Willcuts, supra, 296 U. S. 1, 56 S. Ct. 59, 80 L. Ed. 3, 101 A. L. R. 391, was then new, and we assumed too readily—as we now think—that any income which in fact relieved the husband from alimony was to be regarded as still his. We failed to consider how carefully the opinion in that case had been based upon the Minnesota law, which continued the husband's duty, and in effect made the trust only a security for whatever the divorce court might from time to time allow. We are satisfied that the Supreme Court did not mean to extend the doctrine to situations where the husband's duty is at an end, and to assess him upon income over which he has no control, and in which he has no interest.

The same considerations do not apply to the income of the trust payable to the minor children. Pro tanto the trust was created in performance of Leonard's paternal duty of support, which he could neither commute nor discharge. The payments for 1929 seem to have been calculated on the assumption that nothing was due before August first. The settlement agreement fixed the first of the month next succeeding the date of execution,

as the "settlement date," but that would appear to have been July first, and in any event the provision does not seem to apply to the deed of trust. The proper date would seem to be that on which the deed took effect; but the children were entitled only to that proportion of $5,000 which the remaining months bore to twelve months. The tax will be assessed upon so much as was payable to the minor children so calculated; and the remainder of the deficiency will be expunged.

Order reversed; cause remanded.

155 In United States Circuit Court of Appeals, Second Circuit

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

STEPHEN J. LEONARD, RESPONDENT

STEPHEN J. LEONARD, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appeal from the United States Board of Tax Appeals

Judgment

Filed July 20, 1939

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals, and was argued by counsel.

On consideration whereof, it is now hereby ordered, adjudged, and decreed that the order of said United States Board of Tax Appeals be and it hereby is reversed and cause remanded for further proceedings in accordance with the opinion of this court.

It is further ordered that a Mandate issue to the said Board in accordance with this decree.

D. E. ROBERTS, Clerk.

156 [File endorsement omitted.]

157 [Clerk's certificate to foregoing transcript omitted in printing.]

158 Supreme Court of the United States

Order allowing certiorari

Filed February 5, 1940

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

[Endorsement on cover:] File No. 43833. U. S. Circuit Court of Appeals, Second Circuit. Term No. 426. Guy T. Helvering, Commissioner of Internal Revenue, Petitioner vs. Stephen J. Leonard. Petition for a writ of certiorari and exhibit thereto. Filed September 29, 1939. Term No. 426 O. T. 1939.

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CLERK

No. 426

In the Supreme Court of the United States

OCTOBER TERM, 1939

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

STEPHEN J. LEONARD

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

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In the Supreme Court of the United States

OCTOBER TERM, 1939

No. —

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

STEPHEN J. LEONARD

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

The Solicitor General, on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit, entered in the above-entitled cause on July 20, 1939, reversing the decision of the Board of Tax Appeals.

OPINION BELOW

The opinion of the Board of Tax Appeals (R. 21–39) is reported in 36 B. T. A. 563. The opinion of the Circuit Court of Appeals (R. 152) is not yet reported.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered July 20, 1939 (R. 155–156). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether the taxpayer is taxable upon income payable to his divorced wife for her support and maintenance from a trust created by him, pending her suit for divorce, in connection with a separation agreement which was thereafter approved by the New York divorce decree, even if the divorce court lacked power to award further alimony?

2. In the alternative, whether under New York law the decree of divorce terminated the husband's duty of support and substituted finally therefor the provisions of the agreements incorporated in the decree?

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix, *infra*, pp. 9–12.

STATEMENT

The material facts, as found by the Board of Tax Appeals (R. 23–31), are as follows:

On December 27, 1928 the wife of the taxpayer, who was then living apart from him, began suit for divorce against him in New York (R. 23–24). While this action was pending, the taxpayer and

his wife executed a deed of trust and a separation agreement, both on June 4, 1929 (R. 24, 26).

The deed conveyed securities and cash valued at $650,000 from the taxpayer to a trustee in trust to pay the net income to the beneficiaries therein named in equal monthly installments so far as practicable. (R. 24.) During the life of the wife, the trustee was to pay from the net income $5,000 per year to each of three named children or to the wife as guardian during their minority. The remaining net income was payable to the wife for her support and maintenance. (R. 25.)

The separation agreement incorporated by reference the deed of trust and recited the expectation of both parties that the wife would receive $30,000 per year from the aggregate net income from the trust and from property given to her by the taxpayer in the past. (R. 26–28.) The taxpayer promised to make additional payments of $35,000 per year to his wife for life, provided his circumstances and ability to pay continued as good as of that date, so as to bring the total allowance for her support and maintenance to $65,000 per year. (R. 28.) The wife accepted the establishment of the trust fund and the payments to be made pursuant to the separation agreement in lieu of all dower and released any claim of dower in the property of the taxpayer. (R. 29.)

The divorce decree became final October 22, 1929. The court incorporated the agreements in the de-

cree, "approved and affirmed" the same, and directed the taxpayer to pay his wife $35,000 per annum during her life. (R. 30.)

Between June 4 and December 31, 1929, the trustee received income of $16,191.34 from the trust property. It distributed $5,200 to the wife and five-twelfths of $5,000, or $2,083.33, to each of the three children, leaving an undistributed balance for that period of about $4,700. (R. 31.) The Commissioner included all of this income in the taxpayer's taxable income for 1929. (R. 31, 22–23.) Upon review, the Board of Tax Appeals held that only the amounts actually distributed to taxpayer's wife and minor children were taxable to him and that the portions paid to his adult daughter and undistributed were not so taxable. Both the Commissioner and the taxpayer appealed, and the court below, reversing the decision of the Board, held that although the taxpayer was taxable on income payable to his minor children, he was not taxable on income payable to the wife.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

(1) In holding that the taxpayer was not taxable upon trust income payable to his wife for her support and maintenance under the terms of the trust agreement here involved.

(2) In failing to hold the taxpayer taxable under *Douglas* v. *Willcuts*, 296 U. S. 1.

(3) In holding that *Douglas* v. *Willcuts* is inapplicable unless by state law the divorce court retains power to change its original alimony award.

(4) In not holding that under New York law the terms of the instant divorce decree regarding support of the wife may be changed or modified as justice may require.

(5) In failing to affirm and in reversing the decision of the Board of Tax Appeals insofar as it held that the taxpayer is taxable on trust income paid to his wife.

(6) In affirming and in not reversing the decision of the Board of Tax Appeals insofar as it held the taxpayer not taxable on trust income received in 1929 and currently distributable to the wife but not actually distributed during the taxable year.

REASONS FOR GRANTING THE WRIT

1. This petition presents substantially the same issue as *Helvering* v. *Fitch*, No. 243, present term, in which the Government has applied for a writ of certiorari to review the judgment of the Circuit Court of Appeals for the Eighth Circuit in *Fitch* v. *Commissioner*, 103 F. (2d) 702.

The issue common to this case and to the *Fitch* case is also presented in *Commissioner* v. *Fuller*, decided June 30, 1939, in which a petition for certiorari is also being filed by the Government to review the judgment of the Circuit Court of Appeals for the Second Circuit.

Reference is made to the petition filed in the *Fitch* case for the reasons for granting the writ requested.

There is a difference in the cases in that here a small portion of the trust income was not distributed during the taxable year whereas all of the income involved in the *Fitch* and the *Fuller* cases was actually so distributed. It is thought that this difference has no legal significance and in this respect our view is supported by the decision of the court below, which held (R. 155) that the taxpayer was taxable on income payable to the minor children even though not all of it was distributed during the taxable year. Cf. *Freuler* v. *Helvering*, 291 U. S. 35, 42.

2. The alternative issue to be presented, if certiorari should be granted, is whether the court below correctly held that the provisions of the separation agreement for support of the wife were not subject to alteration after the divorce decree. In so holding, the court below relied upon *Galusha* v. *Galusha*, 116 N. Y. 635, 138 N. Y. 272, a case decided prior to the enactment of Section 21 of the Domestic Relations Law of 1896 (N. Y. Laws, 1896, Vol. 1, c. 272, p. 220) from which was derived Section 51 applicable here. Sections 1155 and 1170 of the New York Civil Practice Act (see Appendix, *infra*) give the divorce court power to change allowances "at any time after final judgment", and Section 51 of the Domestic Relations Law (Appendix, *infra*) provides that a wife cannot contract

to relieve her husband from his liability to support her. Under these statutes, the effect of such an agreement as the one in the instant case is to fix the amount of the husband's liability but not to discharge his obligation. *Winter* v. *Winter,* 191 N. Y. 462, 473–474; *Fox* v. *Fox,* 263 N. Y. 68, 70; *Tirrell* v. *Tirrell,* 232 N. Y. 224; cf. *Lyeth* v. *Hoey,* 305 U. S. 188, 197.

The separation agreement became merged in the judgment of the divorce court which might thereafter be modified as justice should require. *Kunker* v. *Kunker,* 230 App. Div. 641, 644–645 (3d Dept.). Although the court below said that *Kunker* v. *Kunker* seems "at variance with the law" (R. 154), still that case has been consistently followed by the New York courts.[1] It appears that *Kunker* v. *Kunker, supra,* has been approved or followed in all four departments of the Appellate Division of the New York Supreme Court[2]

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[1] See, for example, *Schnitzer* v. *Buerger,* 237 App. Div. 622, 624 (1st Dept.), and *Staehr* v. *Staehr,* 237 App. Div. 843 (2d Dept.).

See also *Goldstein* v. *Goldsmith,* 243 App. Div. 268, 271 (2d Dept.); *Dworkin* v. *Dworkin,* 247 App. Div. 213, 214 (1st Dept.); *Holahan* v. *Holahan,* 234 App. Div. 572, 574 (4th Dept.); *Severance* v. *Severance,* 235 App. Div. 799 (2d Dept.); *Mandel* v. *Mandel,* 235 App. Div. 821 (2d Dept.).

[2] Although *Kunker* v. *Kunker* may be out of harmony with one of the decisions of the Fourth Department cited by the court below (R. 154), namely, *Cain* v. *Cain,* 188 App. Div. 780, it is probably consistent with the other and later one, *Hamlin* v. *Hamlin,* 224 App. Div. 168, 172.

and that it is consistent with the decisions of the Court of Appeals. It is therefore believed that the court below erred in its interpretation of the New York law and in its decision, even assuming *arguendo* that the taxability of the grantor of a so-called alimony trust necessarily depends upon whether his duty of support has finally been terminated by the divorce decree under applicable state law.

CONCLUSION

It is therefore respectfully submitted that this petition for a writ of certiorari should be granted.

ROBERT H. JACKSON,
Solicitor General.

SEPTEMBER, 1939.

APPENDIX

Revenue Act of 1928, c. 852, 45 Stat. 791:

SEC. 22. GROSS INCOME.

(*a*) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

* * * * * *

SEC. 24. ITEMS NOT DEDUCTIBLE.

(*a*) *General rule.*—In computing net income no deduction shall in any case be allowed in respect of—

(1) Personal, living, or family expenses;

* * * * *

Treasury Regulations 74, promulgated under the Revenue Act of 1928:

ART. 83. *Gifts and bequests.*—Property received as a gift, or received under a will or under statutes of descent and distribution, is exempt from the income tax, although the income therefrom derived from investment, sale, or otherwise is not. An amount of principal paid under a marriage settlement is a gift. Neither alimony nor an allowance

based on a separation agreement is taxable income. (See article 281.)

ART. 281. *Personal and family expenses.*— * * * Alimony and an allowance paid under a separation agreement are not deductible from gross income. (See article 83.) * * *

New York Civil Practice Act, Book 6:

§ 1155. *Maintenance and support of wife and children in action for divorce by wife*

The court, in the final judgment dissolving the marriage in an action for divorce brought by the wife, may require the defendant to provide suitably for the education and maintenance of the children of the marriage, and for the support of plaintiff, as justice requires, having regard to the circumstances of the respective parties; and, by order, upon the application of either party to the action, and after due notice to the other, to be given in such manner as the court shall prescribe, at any time after final judgment whether heretofore or hereafter rendered, may annul, vary or modify such a direction. But no such application shall be made by a defendant unless leave to make the same shall have been previously granted by the court by order made upon or without notice as the court in its discretion may deem proper after presentation to the court of satisfactory proof that justice requires that such an application should be entertained.

§ 1170. *Custody and maintenance of children, and support of plaintiff in action for divorce or separation*

Where an action for divorce or separation is brought by either husband or wife, the

court, except as otherwise expressly prescribed by statute, must give, either in the final judgment, or by one or more orders, made from time to time before final judgment, such directions as justice requires, between the parties, for the custody, care, education, and maintenance of any of the children of the marriage, and where the action is brought by the wife, for the support of the plaintiff. The court, by order, upon the application of either party to the action, or any other person or party having the care, custody and control of said child or children pursuant to said final judgment or order, after due notice to the other, to be given in such manner as the court shall prescribe, at any time after final judgment, may annul, vary or modify such directions, or in case no such direction or directions shall have been made, amend it by inserting such direction or directions as justice requires for the custody, care, education and maintenance of any such child or children or for the support of the plaintiff in such final judgment or order or orders. But no such application shall be made by a defendant, or any other person or party having the care, custody and control of said infant or infants, unless leave to make the same shall have been previously granted by the court by order made upon or without notice as the court in its discretion may deem proper after presentation to the court of satisfactory proof that justice requires that such an application should be entertained. (Amended by L. 1921, ch. 199; L. 1925, ch. 240, in effect Sept. 1, 1925.)

The last sentence of Section 1170 was omitted by Laws of 1934, c. 521, in effect September 1.

New York Domestic Relations Law (McKinney's Consolidated Laws of New York, Book 14):

> § 51. *Powers of married woman.*—A married woman has all the rights in respect to property, real or personal, and the acquisition, use, enjoyment and disposition thereof, and to make contracts in respect thereto with any person, including her husband, and to carry on any business, trade or occupation, and to exercise all powers and enjoy all rights in respect thereto and in respect to her contracts, and be liable on such contracts, as if she were unmarried; but a husband and wife cannot contract to alter or dissolve the marriage or to relieve the husband from his liability to support his wife. * * *

The foregoing provisions of the Civil Practice Act and the Domestic Relations Law were in force in 1929 when the trust and separation agreements in this case were executed and the divorce granted; and, except as above indicated, those provisions have not subsequently been altered or amended.

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No. 426

In the Supreme Court of the United States

OCTOBER TERM, 1939

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

STEPHEN J. LEONARD

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE PETITIONER

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OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 11–21) is reported in 36 B. T. A. 563. The opinion of the Circuit Court of Appeals (R. 76–80) is reported in 105 F. (2d) 900.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on July 20, 1939 (R. 80.) The petition for a writ of certiorari was filed September 29, 1939, and was granted February 5, 1940. The

jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether payments to respondent's divorced wife from the income of a trust which was created by him for her maintenance and support and which was ratified in the divorce decree of a New York court should be included in his taxable income.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix, *infra*, pp. 25–28.

STATEMENT

The material facts, as found by the Board of Tax Appeals (R. 12–16), are as follows:

On December 27, 1928, the wife of the taxpayer, who was then living apart from him, began suit for divorce against him in New York. (R. 12.) While this action was pending, the taxpayer and his wife executed a deed of trust and a separation agreement, both on June 4, 1929. (R. 12, 14.)

The deed conveyed securities and cash valued at $650,000 [1] from the taxpayer to a trustee in trust to pay the net income to the beneficiaries therein

[1] Included in that amount were bonds of an aggregate face amount of $400,000 which petitioner himself guaranteed as to principal and interest, and in case of default he agreed to substitute cash or securities in lieu thereof. (R. 13.)

named in equal monthly installments so far as practicable. (R. 12–13.) During the life of the wife, the trustee was to pay from the net income $5,000 per year to each of three named children or to the wife as guardian during their minority. The remaining net income was payable to the wife for her support and maintenance. (R. 13.) Upon the death of the wife, the trust fund was to be divided into as many parts as there were children of the grantor by the wife, each part to constitute a separate trust fund for the benefit of each child as life beneficiary. Upon the death of each life beneficiary, the corpus was to be paid as directed by the will of such beneficiary. (R. 13–14.)

The separation agreement incorporated by reference the deed of trust and recited the expectation of both parties that the wife would receive $30,000 per year from the aggregate net income from the trust and from property given to her by the taxpayer in the past. (R. 14–15.) The taxpayer promised to make additional payments of $35,000 per year to his wife for life, provided his circumstances and ability to pay continued as good as of that date, so as to bring the total allowance for her support and maintenance to $65,000 per year. (R. 15.) The wife accepted the establishment of the trust fund and the payments to be made pursuant to the separation agreement in lieu of all dower and released any claim of dower in the property of the taxpayer. (R. 15.)

The divorce decree became final October 22, 1929.

The court incorporated the agreements in the decree, "approved and affirmed" the same, and directed the taxpayer to pay his wife $35,000 per annum during her life. (R. 16.)

Between June 4 and December 31, 1929, the trustee received income of $16,191.34 from the trust property. It distributed $5,200 to the wife and five-twelfths of $5,000, or $2,083.33, to each of the three children, leaving an undistributed balance for that period of about $4,700. (R. 16.) The Commissioner included all of this income in the taxpayer's taxable income for 1929. (R. 16, 11–12.) Upon review, the Board of Tax Appeals held that only the amounts actually distributed to taxpayer's wife and minor children were taxable to him and that the portions paid to his adult daughter and undistributed were not so taxable. Both the Commissioner and the taxpayer appealed, and the court below, reversing the decision of the Board, held that although the taxpayer was taxable on income payable to his minor children, he was not taxable on income payable to the wife.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that the taxpayer was not taxable upon trust income payable to his wife for her support and maintenance under the terms of the trust agreement here involved.

2. In failing to hold the taxpayer taxable under *Douglas* v. *Willcuts*, 296 U. S. 1.

3. In holding that *Douglas* v. *Willcuts* is inapplicable unless by state law the divorce court retains power to change its original alimony award.

4. In not holding that under New York law the terms of the instant divorce decree regarding support of the wife may be changed or modified as justice may require.

5. In failing to affirm and in reversing the decision of the Board of Tax Appeals in so far as it held that the taxpayer is taxable on trust income paid to his wife.

6. In affirming and in not reversing the decision of the Board of Tax Appeals in so far as it held the taxpayer not taxable on trust income received in 1929 and currently distributable to the wife but not actually distributed during the taxable year.

SUMMARY OF ARGUMENT

The trust was created for the purpose of discharging taxpayer's subsisting obligation to support his wife. It was ratified by the divorce court as a means by which he was to discharge that duty after the divorce. The income from the trust is therefore taxable to the taxpayer, just as though he had received it and then paid it over to his wife. *Douglas* v. *Willcuts*, 296 U. S. 1.

That the divorced wife must look solely to the trust is immaterial. It was the act of the taxpayer which permanently devoted the trust income to his obligation. The trust itself is in substance equivalent to a continuing exercise by the settlor

of the power to direct the application of the income along the predetermined channels.

There is no essential difference between the case at bar and *Douglas* v. *Willcuts*. Although the Minnesota court in *Douglas* v. *Willcuts* had the power to modify the alimony decree thereafter, the fact that such continuing power of modification may be absent in New York is inconsequential. In any event, however, the New York law does permit the divorce court to alter the alimony decree, so that even this alleged difference between *Douglas* v. *Willcuts* and the instant case vanishes.

ARGUMENT

THE TRUST INCOME IS TAXABLE TO THE HUSBAND UNDER THE DOCTRINE OF *DOUGLAS* v. *WILLCUTS*

Introductory.—Taxpayer and his wife executed a deed of trust and a separation agreement on June 4, 1929, when the wife's suit for a divorce was pending. The trust deed provided for certain payments to their children, with the remaining net income payable to the wife for her support and maintenance. (R. 13–14.) The divorce decree, which became final October 22, 1929, incorporated the agreements and "approved and affirmed" them. (R. 16.)

The court below held that the amounts payable to the wife from the trust were not includible in taxpayer's income. In reaching that result, the Circuit Court of Appeals interpreted the doctrine of *Douglas* v. *Willcuts*, 296 U. S. 1, as embracing only those "alimony trust" situations in which the

divorce court, by the terms of its decree or the applicable state law, retains the power to change its original award. Having so construed *Douglas* v. *Willcuts,* the court ruled that under the law of New York the divorce court retained no continuing power to modify the provisions for the wife, and accordingly gave judgment in favor of the taxpayer.

In *Helvering* v. *Fitch,* decided January 29, 1940, No. 243, this Court held that the income from the "alimony trust" there involved was taxable to the husband under the general rule enunciated in *Douglas* v. *Willcuts.* In the presentation of the *Fitch* case, the Government argued, first, that the existence of a continuing power in the divorce court to modify the provision for the wife is not a necessary condition to the applicability of *Douglas* v. *Willcuts,* and that, in any event, under applicable Iowa law the divorce court retained the power to modify. This Court held in favor of the Government on the ground that the taxpayer had failed to show by clear and convincing proof that the Iowa court had no continuing jurisdiction, without passing upon the Government's contention that *Douglas* v. *Willcuts* should apply regardless of the local law as to power of the divorce court to change its original award.

1. Assuming, *arguendo,* that the court below was correct in holding that under the law of New York the divorce court retained no continuing power, we again respectfully submit that *Douglas* v. *Willcuts*

should nevertheless control, that there is a functional identity between the two trusts which should not be subject to diverse tax consequences.

In *Douglas* v. *Willcuts*, a husband, in anticipation of divorce, had created a trust for his wife to pay her $15,000 a year for a fixed period, and $21,000 a year thereafter. Excess income was to be paid to him, but in the event of any deficiency in income the trustee could call upon him for the difference, and upon his failure to pay the difference the trustee was authorized to make up the deficiency out of corpus. The parties had agreed that these provisions for the wife were "in lieu of, and in full settlement of alimony, and of any and all dower rights or statutory interests in the estate" of her husband, and "in lieu of any and all claims for separate maintenance and allowance for her support" (p. 3). A divorce decree entered thereafter provided that the provisions in the trust for the wife's benefit were to be in lieu of all alimony or interest in the property of the husband. In holding the husband taxable with respect to the income of that trust, this Court said (pp. 8–9):

> Amounts paid to a divorced wife under a decree for alimony are not regarded as income of the wife but as paid in discharge of the general obligation to support, which is made specific by the decree. * * * Petitioner's contention that the district court did not award alimony is not supported by the terms of the decree. It described the provision as made "in lieu of all *other*

alimony or interest in the property or estate of the defendant." However designated, it was a provision for annual payments to serve the purpose of alimony, that is, to assure to the wife suitable support. The fact that the provision was to be in lieu of any other interest in the husband's property did not affect the essential quality of these payments. Upon the preexisting duty of the husband the decree placed a particular and adequate sanction, and imposed upon petitioner the obligation to devote the income in question, through the medium of the trust, to the use of his divorced wife.

* * * We have held that income was received by a taxpayer, when, pursuant to a contract, a debt or other obligation was discharged by another for his benefit. * * * The creation of a trust by the taxpayer as a channel for the application of the income to the discharge of his obligation leaves the nature of the transaction unaltered. *Burnet* v. *Wells, supra.* In the present case, the net income of the trust fund, which was paid to the wife under the decree, stands substantially on the same footing as though he had received the income personally and had been required by the decree to make the payment directly.

These principles have been applied in a large number of cases: *Helvering* v. *Coxey,* 297 U. S. 694, reversing *per curiam* 79 F. (2d) 661 (C. C. A. 3d); *Helvering* v. *Schweitzer,* 296 U. S. 551, reversing *per curiam* 75 F. (2d) 702 (C. C. A. 7th), rehearing

denied, 296 U. S. 665; *Helvering* v. *Stokes*, 296 U. S. 551, reversing *per curiam* 79 F. (2d) 256 (C. C. A. 3d), rehearing denied, 296 U. S. 665; *Helvering* v. *Blumenthal*, 296 U. S. 552, reversing *per curiam* 76 F. (2d) 507 (C. C. A. 2d); *Donnelley* v. *Commissioner*, 101 F. (2d) 879 (C. C. A. 7th), certiorari denied, 307 U. S. 645; *Glendinning* v. *Commissioner*, 97 F. (2d) 51 (C. C. A. 3d); *Alsop* v. *Commissioner*, 92 F (2d) 148 (C. C. A. 3d), certiorari denied, 302 U. S. 767, rehearing denied, 303 U. S. 666; *Hill* v. *Commissioner*, 88 F. (2d) 941 (C. C. A. 8th); *Commissioner* v. *Grosvenor*, 85 F. (2d) 2 (C. C. A. 2d).

The law of New York imposed upon the taxpayer the obligation to support his divorced wife. New York Civil Practice Act, Ann., Book 6, Sections 1170, 1155, Appendix, *infra*, pp. 26–27. The decree of the divorce court incorporated, "approved and affirmed" the separation agreement, which in turn incorporated the trust. To paraphrase *Douglas* v. *Willcuts*, the decree of the divorce court placed a particular and adequate sanction upon the husband's preexisting duty and required him to discharge his obligation by devoting the income in question, through the medium of the trust, to the use of his divorced wife. That income stands substantially on the same footing as though he had received it personally and discharged his obligation by paying it over to his wife. Here, as in *Douglas* v. *Willcuts*, the trust income serves as a substitute for payments made directly by the hus-

band, and confers on him in every real sense a direct benefit which constitutes taxable income.

The court below, however, undertook to distinguish *Douglas* v. *Willcuts* on the ground that under Minnesota law the divorce court was empowered, at any time after the divorce, to modify the alimony decree, whereas under New York law, no such power was thought to exist. Hence, the court reasoned, there was no continuing obligation on the husband to the satisfaction of which the trust income was devoted. But it is manifestly not essential to the existence of a continuing obligation that the amount thereof be subject to *increase*. If there is a continuing obligation, income devoted to its satisfaction is taxable to the obligor whether the amount of the obligation be subject to modification or be inalterably fixed.[2]

In the instant case, even though there was no recourse against the husband beyond the terms of the trust, he was nevertheless subject to a continuing obligation to support his divorced wife. Under the law of New York, the husband's obligation of support did not terminate upon the granting of an

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[2] Thus, it is clear that if A is legally obligated to pay B $5,000 and no more annually during B's life, and the payments to B are made by C, A realizes income in the amount of the payments by C to B for his benefit. Cf. *Old Colony Tr. Co.* v. *Commissioner*, 279 U. S. 716; *United States* v. *Boston & M. R. Co.*, 279 U. S. 732. The result is the same where taxpayer creates a trust the income of which is applied to the discharge of his obligation. *Helvering* v. *Blumenthal*, 296 U. S. 552. Cf. *Burnet* v. *Wells*, 289 U. S. 670.

absolute divorce. *Daggett* v. *Daggett,* 5 Paige (N. Y.) 509; *Hamlin* v. *Hamlin,* 230 N. Y. S. 51. On the contrary, the New York statute expressly provided that in an action for divorce brought by the wife "the court * * * must give, either in the final judgment, or by one or more orders, made from time to time before final judgment, such directions as justice requires * * * for the support of the plaintiff". New York Civil Practice Act, Book 6, Section 1170. See also Section 1155, Appendix, *infra.* In decreeing alimony, the divorce court merely makes specific the husband's general and continuing obligation to support the wife. *Audubon* v. *Shufeldt,* 181 U. S. 575, 577; *Romaine* v. *Chauncey,* 129 N. Y. 566, 570. If the court, in its final order, had simply ordered the payment to the wife of a designated annual income, the husband's obligation would assuredly have been a continuing one, regardless of the assumed inability of the court to change such order.

The situation is no different because the court adopted the agreement of the parties. An agreement as to the support of the wife will be upheld by the divorce court only if its provisions are fair and equitable, for the husband's continuing obligation to support the wife as long as she lives can not be avoided by an unconscionable contract. *Daggett* v. *Daggett, supra; Hamlin* v. *Hamlin, supra.* Thus, in adopting the agreement, the New York court simply ruled in substance that the just provision for the wife, which it was required by

statute to order, coincided with what the parties had themselves arranged. Accordingly, the court ordered the husband to do as he had agreed. But the fact that the court, in delineating the extent of the husband's future liability, determined it as coextensive with what the parties had agreed did not terminate the husband's obligation. The court's acceptance of the parties' agreement merely indicated that the court believed its provisions were "as justice requires". Had the court deemed the agreement unjust, it could have imposed on the husband an additional or different continuing obligation.

The decree of the court recognized the husband's preexisting duty to support, and defined that duty as coextensive with what the parties had themselves arranged. Thus, the trust income served to satisfy and discharge the husband's continuing obligation under the law of New York, as defined in the final order by the court. We submit that such income is therefore taxable to the husband. The fact that in the *Douglas* case the Minnesota court could later modify its final decree provided a striking illustration of the fact that the trust income was there devoted to the discharge of taxpayer's continuing obligation, but that circumstance was not essential to the decision. *The critical element is that the duty to support after divorce existed at the time the trust was executed, and the grantor simply carved out future income*

from property which he then owned and devoted it in advance to the discharge of that obligation.

The Court in *Douglas* v. *Willcuts* likewise commented at some length (296 U. S. 1, 8) upon the fact that the Minnesota court—

> did not approve the trust agreement as one deriving efficacy from the action of the parties. The court made its own requirement. The decree required the petitioner to "provide and create the trust fund." While the terms of the trust as set up in the trust agreement were approved, the court made those terms its own. It was from this action of the court that the trust derived its force.

Yet, within three months, in *Helvering* v. *Coxey*, 297 U. S. 694, the Court ruled *per curiam* that the grantor of an alimony trust was taxable, even though the decree of the state court made no mention whatever of the trust. We believe that the continuing power of the Minnesota court, together with the grantor's contingent liability to make up deficiencies, were no more essential to the decision in *Douglas* v. *Willcuts* than was the fact that the Minnesota court ratified and adopted the trust.

The important consideration in *Douglas* v. *Willcuts* was, we submit, that the trust operated to discharge the taxpayer's obligation to his wife, whether or not that obligation could be increased, or whether or not it was fortified by a contingent liability to make up deficiencies. In New York, as in Minnesota, the divorce court may mark out the husband's duty of future maintenance, and

enter an appropriate order. And where the court determines that the income from a trust established by the husband is adequate provision for such maintenance, the subsequent application of that income carries out that obligation, and should be taxable to the husband.

This case differs from *Douglas* v. *Willcuts* only as to the *extent* of the obligation, rather than its *continued existence.* In both situations the husband had, at the time of the divorce decree, an obligation toward his wife. In both cases, the divorce court marked out the limits of that obligation. In *Douglas* v. *Willcuts,* that obligation was subject to possible increase by the divorce court, whereas we are assuming that the divorce court in the present case lacked such power. But in each case, the income was applied to the discharge of the obligation recognized by the divorce court. And in both, the trusts were merely the predetermined channels for the application of the income to the discharge of the husband's duty to support. The absence of power in the divorce court to decree an expansion of the extent of that duty does not change the essential quality of the trust income as applied in lieu of alimony.

With regard to the extent of the obligation, as distinguished from its *continuance,* the instant case differs further from *Douglas* v. *Willcuts* in that the husband here did not undertake to make good deficiencies in the income of the trust. However, we contend that *Douglas* v. *Willcuts* is applicable

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irrespective of a guaranty by the husband against deficiency in trust income. It is true that, in stating the facts in the *Douglas* case, this Court briefly mentioned that "Deficiencies were to be made up in a prescribed manner" (296 U. S. 3), but that fact was not even adverted to in the remainder of the opinion and we submit it was not necessary to the result.

If the applicability of *Douglas* v. *Willcuts* is made dependent upon an undertaking to make up deficiencies in trust income, the emasculation of the vital principle of the case would assuredly result. Tax liability could readily be avoided while substantially guaranteeing the wife's income from the trust by a variety of artful provisions in the trust instrument. The husband, while refraining from an express guaranty that the wife would receive a designated sum annually, could guarantee the principal and interest on bonds constituting the entire trust corpus. This was almost the situation in the instant case, where the husband guaranteed bonds, both as to principal and interest, of a value of $400,000 out of a total trust corpus of $650,000. (R. 12–13.) Or, in conjunction with the establishment of a trust, the husband might agree personally to pay the wife in addition a specified sum, say $20,000 per year, subject to modification from time to time by the divorce court, depending on circumstances. Any decrease in the trust income would undoubtedly be a factor to be considered by the

court in determining the amount of the additional payments from the husband.[3] Similarly, a husband desirous of providing an annual income for the divorced wife of $5,000 might create a trust of such size that its normal income would be $10,000 and provide that from the trust income $5,000 was first to be paid to the wife, and the balance to him, thereby affording the wife a comfortable margin of security that her alimony would be paid.[4] Likewise, the trust instrument might provide that if the trust income fell below the amount payable to the divorced wife, the husband would assign certain

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[3] The instant case does in fact involve a similar feature. By the terms of the separation agreement approved and incorporated in the final decree, the husband was to pay the wife $35,000 per year, subject to reduction to not less than $10,000 by the divorce court. (R. 36.) Although the agreement makes the husband's circumstances and ability to pay the test for granting any reduction, as pointed out by the court below (R. 78), the divorce court might take into account the wife's other means, in which case any diminution in income from the trust would be a factor in determining the amount of the payments from the husband. Should the amount payable annually be once reduced from the maximum of $35,000 permitted by the agreement any subsequent decrease in trust income might be reflected in an increase in the husband's personal liability.

[4] Such a situation obtained in *Helvering* v. *Fitch*, *supra*, decided January 29, 1940, where the trust income was $12,000 per year, of which only $7,200 was payable to the wife, with the remainder going to the husband. Yet one of the reasons for which the Circuit Court of Appeals for the Eighth Circuit held that *Douglas* v. *Willcuts* was inapplicable was the absence of an undertaking to make up deficiencies. 103 F. (2d) 702.

designated securities to the trust to make up the deficiency.[5]

By adroit utilization of any of the foregoing, or similar, arrangements, or a combination of two or more of them, the husband in nearly every case could substantially insure his wife a specified annual income without personally assuming responsibility to make up any deficiencies. As a practical matter, the difference between such a situation and *Douglas* v. *Willcuts* would be negligible. Yet if liability to make up a hypothetical deficiency is regarded as essential, the husband in such a situation would not be subject to tax. We believe that this Court could not have intended *Douglas* v. *Willcuts* to be thus drastically limited by so attenuated and meaningless a distinction.

Moreover, the result reached below permits the husband to circumvent an express prohibition in the statute and regulations. Section 24 (a) (1), of the Revenue Act of 1928, Appendix, *infra,* provides that no deduction shall be allowed in respect of "Personal, living, or family expenses", and Article 281 of Regulations 74, *infra,* construing the statute, provides that alimony may not be deducted from gross income. Had the grantor held the property without the interposition of the trust, and

[5] This was the situation in *Dixon* v. *Commissioner* (C. C. A. 3d), decided January 10, 1940, not yet officially reported but found in 1940 C. C. H., Vol. 4, p. 9462, in which it was held that *Douglas* v. *Willcuts* was inapplicable because there was no personal guaranty by the husband of the wife's income.

simply paid out the income therefrom to his wife as alimony he would have been chargeable with the full amount of that income and would not have been entitled to any deduction on account of the alimony paid out. The decision below permits him to achieve the same result by creating a trust, but without rendering him liable for tax with respect to the income. In essence, it awards him the very deduction that Congress has denied him.

Furthermore, the basic issue before the Court is whether the income in question falls within the definition of gross income as set forth in Section 22 (a), *infra*, and the broad sweep of that definition has often been said to be coextensive with the power of Congress under the Constitution. *Helvering* v. *Stockholms &c. Bank*, 293 U. S. 84, 89; *Douglas* v. *Willcuts*, *supra*, at p. 9; *United States* v. *Safety Car Heating Co.*, 297 U. S. 88, 93; *Helvering* v. *Midland Ins. Co.*, 300 U. S. 216, 223; *Irwin* v. *Gavit*, 268 U. S. 161, 166; *Helvering* v. *Clifford*, No. 383, present Term, decided February 26, 1940. However, it seems clear beyond question that there can be no constitutional objection to the tax here involved. For, in *Burnet* v. *Wells*, 289 U. S. 670, this Court sustained a tax upon the grantor of an irrevocable trust established to pay premiums on policies of insurance taken out on his own life for the benefit of others. No legal obligation of any kind was there involved. At most the trust served to discharge a moral obligation owed by the grantor to his family. Yet it accomplished a result which

to him was desirable, and which he would otherwise have been compelled to achieve by the use of his own funds or unrestricted income. By employing an irrevocable trust, he had merely devoted a portion of his future income to that end. The Court commented upon the various trust devices employed in order to defeat taxes in which the common element was the surrender of title to another while retaining the substance of enjoyment. And in sustaining the tax, the Court remarked (p. 677):

> At times escape has been blocked by the resources of the judicial process without the aid of legislation. * * * In these and other cases there has been a progressive endeavor by the Congress and the courts to bring about a correspondence between the legal concept of ownership and the economic realities of enjoyment or fruition. * * *

2. Thus far, we have urged that *Douglas* v. *Willcuts* applies without regard to the continued power of the divorce court to modify the decree or the existence of a contingent obligation to make up any hypothetical deficiencies in trust income. And for the purpose of argument we assumed that the court below had correctly interpreted the New York law as forbidding any subsequent modifications of the alimony decree. However, we believe that the court erred in its interpretation of the New York law, and that the power to modify does exist in New York.

Sections 1155 and 1170 of the New York Civil Practice Act, Appendix, *infra*, specifically and un-

equivocally confer on the divorce court the power to "annul, vary or modify" its direction for the support of the wife "at any time after final judgment". Moreover, Section 51 of the New York Domestic Relations Law, Appendix, *infra,* forbids a wife from making an agreement discharging her husband's duty to support her. The court below referred to these statutory provisions (R. 78), but held that nevertheless, under the New York decisions, a settlement is finally binding upon the parties in the absence of fraud, duress, etc.

In so holding, the court relied upon *Galusha* v. *Galusha,* 116 N. Y. 635. But that case was decided prior to the enactment of Section 21 of the Domestic Relations Law of 1896 (New York Laws, 1896, Vol. 1, c. 272, p. 220) from which was derived Section 51, applicable here. Moreover, that case appears to be inconsistent with *Daggett* v. *Daggett,* 5 Paige (N. Y.) 509, not there overruled, which was cited with approval and followed, after the *Galusha* decision, in *Dailey* v. *Dailey,* 9 Misc. (N. Y.) 511, 514. The only other authorities upon which the court below based its conclusion as to the New York law are *Cain* v. *Cain,* 188 App. Div. (N. Y.) 780, and *Hamlin* v. *Hamlin,* 224 App. Div. (N. Y.) 168, both decided by the Fourth Department of the Appellate Division of the New York Supreme Court. Although the *Cain* case does appear to afford some support for the court's view of the New York law, the later *Hamlin* case held that an agreement providing for the support of the

wife could be modified by the divorce court where its terms were inadequate and unfair.

Under the New York statute, although the final judgment of divorce ends the relationship of husband and wife, the husband's obligation of support is continued in the form of alimony, and the court's jurisdiction over the parties and the incidental subject matter does not terminate. *Fox* v. *Fox*, 263 N. Y. 68, 70; *Winter* v. *Winter*, 191 N. Y. 462, 473–474. Moreover, an agreement providing for the wife will be set aside if unfair and unequitable. *Hamlin* v. *Hamlin*, 224 App. Div. (N. Y.) 168; cf. *Tirrell* v. *Tirrell*, 232 N. Y. 224; *Hungerford* v. *Hungerford*, 161 N. Y. 550.

In *Kunker* v. *Kunker*, 230 App. Div. (N. Y.) 641, the Appellate Division of the Supreme Court, Third Department, expressly held that the court has power to modify its judgment, in an action for absolute divorce, and change the provision for support, notwithstanding an agreement for support was incorporated and approved in the final decree. The court declared that upon the incorporation of the agreement in the judgment, it became a part thereof, and that the statutory power to modify the judgment is not divested merely because it was based on a formal agreement rather than a stipulation or evidence. This case is squarely in point, and sustains our contention that the divorce court in the present case retained the power to modify the provision for the wife. The court below dismissed *Kunker* v. *Kunker* as a mere aberration, at

variance with New York decisions. The fact remains, however, that the *Kunker* case has been consistently followed by the New York courts,[6] has been approved or followed in all four departments of the Appellate Division of the New York Supreme Court,[7] and is consistent with the decisions of the Court of Appeals.

We believe that the clear language of the New York statutes (Sections 1155 and 1170) of the Civil Practice Act, and Section 51 of the Domestic Relations Law), together with the foregoing decisions, particularly *Kunker* v. *Kunker,* established clearly that the New York law empowered the divorce court to modify the provisions for the wife contained in its final decree. But in any event, under the decision of this Court in the *Fitch* case, the burden is on the taxpayer to show, "by clear and convincing proof" that under the New York law the divorce court retains no power to modify. At most, that conclusion could be based on no more than "mere

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[6] See, for example, *Schnitzer* v. *Buerger*, 237 App. Div. 622, 624 (1st Dept.), and *Staehr* v. *Staehr*, 237 App. Div. 843 (2d Dept.).

See also *Goldstein* v. *Goldsmith*, 243 App. Div. 268, 271 (2d Dept.); *Dworkin* v. *Dworkin*, 247 App. Div. 213, 214 (1st Dept.); *Holahan* v. *Holahan*, 234 App. Div. 572, 574 (4th Dept.); *Severance* v. *Severance*, 235 App. Div. 799 (2d Dept.); *Mandel* v. *Mandel*, 235 App. Div. 821 (2d Dept.).

[7] Although *Kunker* v. *Kunker* may be out of harmony with one of the decisions of the Fourth Department cited by the court below (R. 78), namely, *Cain* v. *Cain*, 188 App. Div. 780, it is probably consistent with the other and later one, *Hamlin* v. *Hamlin*, 224 App. Div. 168, 172.

inferences and vague conjectures", in the face of plainly contrary statutory language. Accordingly, under the rule announced in *Helvering* v. *Fitch*, the instant case is governed by *Douglas* v. *Willcuts*.

CONCLUSION

The decision of the court below should be reversed.

Respectfully submitted.

FRANCIS BIDDLE,
Solicitor General.
SAMUEL O. CLARK, JR.,
Assistant Attorney General.
SEWALL KEY,
ARNOLD RAUM,
HOWARD D. PACK,
Special Assistants to the Attorney General.

MARCH 1940.

APPENDIX

Revenue Act of 1928, c. 852, 45 Stat. 791:

SEC. 22. GROSS INCOME.

(a) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

* * * * *

SEC. 24. ITEMS NOT DEDUCTIBLE.

(a) *General rule.*—In computing net income no deduction shall in any case be allowed in respect of—

(1) Personal, living, or family expenses;

* * * * *

Treasury Regulations 74, promulgated under the Revenue Act of 1928:

ART. 83. *Gifts and bequests.*—Property received as a gift, or received under a will or under statutes of descent and distribution, is exempt from the income tax, although the income therefrom derived from investment, sale, or otherwise is not. An amount of principal paid under a marriage settlement is a gift. Neither alimony nor an allowance

based on a separation agreement is taxable income. (See article 281.)

ART. 281. *Personal and family expenses.*—* * * Alimony and an allowance paid under a separation agreement are not deductible from gross income. (See article 83.) * * *

New York Civil Practice Act, Book 6:

§ 1155. *Maintenance and support of wife and children in action for divorce by wife*

The court, in the final judgment dissolving the marriage in an action for divorce brought by the wife, may require the defendant to provide suitably for the education and maintenance of the children of the marriage, and for the support of the plaintiff, as justice requires, having regard to the circumstances of the respective parties; and, by order, upon the application of either party to the action, and after due notice to the other, to be given in such manner as the court shall prescribe, at any time after final judgment whether heretofore or hereafter rendered, may annul, vary or modify such a direction. But no such application shall be made by a defendant unless leave to make the same shall have been previously granted by the court by order made upon or without notice as the court in its discretion may deem proper after presentation to the court of satisfactory proof that justice requires that such an application should be entertained.

§ 1170. *Custody and maintenance of children, and support of plaintiff in action for divorce or separation*

Where an action for divorce or separation is brought by either husband or wife, the

court, except as otherwise expressly prescribed by statute, must give, either in the final judgment, or by one or more orders, made from time to time before final judgment, such directions as justice requires, between the parties, for the custody, care, education, and maintenance of any of the children of the marriage, and where the action is brought by the wife, for the support of the plaintiff. The court, by order, upon the application of either party to the action, or any other person or party having the care, custody and control of said child or children pursuant to said final judgment or order, after due notice to the other, to be given in such manner as the court shall prescribe, at any time after final judgment, may annul, vary or modify such directions, or in case no such direction or directions shall have been made, amend it by inserting such direction or directions as justice requires for the custody, care, education and maintenance of any such child or children or for the support of the plaintiff in such final judgment or order or orders. But no such application shall be made by a defendant, or any other person or party having the care, custody and control of said infant or infants, unless leave to make the same shall have been previously granted by the court by order made upon or without notice as the court in its discretion may deem proper after presentation to the court of satisfactory proof that justice requires that such an application should be entertained. (Amended by L. 1921, ch. 199; L. 1925, ch. 240, in effect Sept. 1, 1925.)

The last sentence of Section 1170 was omitted by Laws of 1934, c. 521, in effect September 1.

New York Domestic Relations Law (McKinney's Consolidated Laws of New York, Book 14):

> § 51. *Powers of married woman.*—A married woman has all the rights in respect to property, real or personal, and the acquisition, use, enjoyment and disposition thereof, and to make contracts in respect thereto with any person, including her husband, and to carry on any business, trade or occupation, and to exercise all powers and enjoy all rights in respect thereto and in respect to her contracts, and be liable on such contracts, as if she were unmarried; but a husband and wife can not contract to alter or dissolve the marriage or to relieve the husband from his liability to support his wife. * * *

The foregoing provisions of the Civil Practice Act and the Domestic Relations Law were in force in 1929 when the trust and separation agreements in this case were executed and the divorce granted; and, except as above indicated, those provisions have not subsequently been altered or amended.

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Supreme Court of the United States

OCTOBER TERM, 1939.

No. 426.

GUY T. HELVERING, Commissioner of Internal Revenue,

Petitioner,

—against—

STEPHEN J. LEONARD,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR THE RESPONDENT.

J. DONALD DUNCAN,
Attorney for the Respondent.

JAMES B. ALLEY,
JAMES T. BREDIN,
Of Counsel.

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ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR THE RESPONDENT.

Opinions Below.

The opinion of the Board of Tax Appeals (R. 11-21) is reported in 36 B. T. A. 563. The opinion of the Circuit Court of Appeals (R. 76-80) is reported in 105 F. (2d) 900.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered on July 20, 1939 (R. 80). The petition for a writ of certiorari was filed September 29, 1939, and was granted February 5, 1940. The jurisdiction of this Court rests on Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

Question Presented.

Whether payments to respondent's divorced wife and children of income derived from that part of the principal contributed by the husband to the aggregate assets of both husband and wife which were set aside pursuant to the terms of an irrevocable contract of trust executed by both the husband and his wife with a trust company as trustee, should be included in the respondent husband's taxable income.

Statutes and Regulations Involved.

The statutes and regulations involved are set forth in the Appendix, *infra*, pages 33-36.

Statement.

The facts in this case are as follows:

On December 27, 1928 the wife of the taxpayer began a suit for divorce from him in the State of New York (R. 12). There were three children of the parties to the divorce action two of whom Stephanie and Craig were minors throughout the taxable year in question and one, Jeanne, became 21 years of age on July 18, 1929 (R. 12).

On the 4th day of June, 1929 two documents were executed by the taxpayer and his wife. One was a separation agreement, the other was an agreement or contract of trust executed with the United States Trust Company of New York as Trustee (R. 12, 14) and is hereinafter referred to as the trust agreement.

The agreement of trust is set forth in the record beginning at the bottom of page 38 to page 50. The taxpayer is therein referred to as the grantor and his wife is referred to as the third party. The principal of the trust was contributed to by both the taxpayer

and his wife, the taxpayer contributing an aggregate principal value of $650,000 (R. 39) and the wife three life insurance policies which she owned upon the life of the taxpayer in the principal amount of $100,000 each for an aggregate principal of $300,000 (R. 48), the premiums upon which were payable by the wife.

During the life of the wife the trustee was directed to pay from the net income of the trust $5000 per year to each of the three named children except that during the minority of any child the $5000 for the child was to be paid to the wife as guardian, and if any said child should die during the life of the wife the $5000 payable to said child should thereafter be paid to the wife during her life for her own separate use (R. 46). Any income in excess of $15,000 was directed to be paid to the wife during her life (R. 13), to be used by her for her maintenance and support and in her sole discretion for the support, maintenance and education of the children (R. 46). Upon the death of the wife the principal was divisible into as many parts as there were children of the grantor by the wife, each part to constitute a separate trust fund for the benefit of each child as life beneficiary. Upon the death of each life beneficiary the principal was to be paid as appointed in the will of the beneficiary or in default of such appointment to his or her issue and in default of such issue then to the descendants of the wife by the husband and if there were no such issue then to the descendants of the husband (R. 47).

The trust agreement also provided that it could be amended by the husband and the wife and it was amended subsequently on the 10th of December, 1929; again on November 17, 1930; and again on the 23rd of June, 1932 without any action by any court (R. 54 to 72).

The separation agreement is set forth at pages 33 to 38 of the Record. It referred to the fact that the taxpayer and his wife had entered into the aforesaid trust agreement with the United States Trust Company of New York as Trustee and (R. 34) recited (a) that the net income from the trust subject to a prior charge of $15,000 in favor of the three children was payable to the wife; (b) that the wife had received in the past in addition to any interest in the trust fund and by way of gifts from the husband personal property of the value of $350,000 which the wife agreed to then have a present income value of at least $15,000 so (c) that the wife agreed that as of the date of the execution of the separation agreement she had an income of at least $30,000 a year from said gifts and from the trust fund. Thereafter by further terms of the separation agreement (R. 35) the taxpayer agreed to pay to his wife for life for her support and maintenance and for the support of the three children the sum of $35,000 per year in equal monthly payments beginning with the month of July, 1929, and in addition any extraordinary medical or surgical expenses incurred by the wife individually or by her on behalf of the three children until the time when each child should respectively attain the age of 25 years (R. 35 and 36). The separation agreement also stated that the husband should not in any way be responsible for any diminution of the net income receivable by the wife by reason of any decrease in income from the property theretofore given to the wife or from the trust fund except to any extent necessary to make good the value of the bonds of the McCulloch Oil Company deposited by him in the trust fund.

Provision was made in the separation agreement that if the husband's ability to pay the aforesaid $35,000 alimony should be impaired he should have

the right to apply to any court of competent jurisdiction for a reduction of his obligation to pay $35,000 to not less than $10,000 per year and the extraordinary medical or surgical expenses but no such application should be made within two years of the date of the execution of the agreement and if at any time the $35,000 should be reduced by a court and thereafter the financial circumstances of the husband should improve so that he should once more be able to pay $35,000 per year, the wife had the right to apply to any court of competent jurisdiction for an increase in the amount then being paid by the husband provided that any increase which might be granted should not cause the husband to pay the wife a greater amount in the aggregate than $35,000 per year (R. 36).

All the personal property appurtenant to the real property and dwellings of the parties in Long Island and in the apartment at Park Avenue, New York, was confirmed to be the property of the wife and the husband released any and all claim thereto. The sole care, custody and control of the children was given to the wife except that the husband had the right to visit the children at all reasonable times. The wife agreed to accept the execution of the contract of trust and the payments to be made by the husband pursuant to the separation agreement in lieu of all dower and released the husband and his estate from any claim of dower in his property (R. 37-38).

The divorce case was prosecuted and the decree of the divorce court which is set forth at pages 51-52 of the Record became final October 22, 1929. *This decree approved the separation agreement, did not mention the trust agreement,* granted the sole care, custody and control of the children to the wife and ordered the husband to pay her for and during the

term of her natural life the sum of $35,000 per year (R. 52).

Between the date of the establishment of the trust in June and the end of the calendar year 1929 the United States Trust Company as Trustee collected net income from the principal of the trust agreement of $16,191.34. According to the testimony of an official of said Trust Company it reported the income for income tax purposes (R. 32) as payable to the extent of $15,000 of $5,000 each to each of the three children but for some reason which the aforesaid official of the Trust Company could not explain, up to December 31, 1929 (R. 31) the Trust Company paid only $2,033.33 to each of the three children; $5,200 to the wife and did not distribute the remaining $4,700 (R. 30-31).

The Commissioner included the entire $16,191.34 of net income in the husband's taxable income for the year 1929 (R. 16, 11-12). Upon review the Board of Tax Appeals held that the amounts actually distributed to the wife and minor children were taxable to the husband and the amounts paid the adult daughter and undistributed by the trustee were not so taxable. Both the Commissioner and the taxpayer appealed and the court below held that although the taxpayer was taxable on the income payable to the minor children, he was not taxable on the income payable to the wife.

Specification of Error to Be Urged.

The Circuit Court of Appeals erred in holding that the husband was taxable upon the amounts of income from the principal of the trust agreement which were payable to the minor children of the husband and his divorced wife.

Summary of Argument.

The divorce decree approved and affirmed and made a part of the judgment the *separation agreement* providing for the maintenance and support of the taxpayer's divorced wife and children; directed that the taxpayer's divorced wife have the sole care, custody and control of the taxpayer's children and that the taxpayer pay to his divorced wife the sum of $35,000 per year, as provided for in the separation agreement.

The decree did not affirm, approve or in any manner deal with the *trust agreement*, the creation of which was a contract of the taxpayer and his wife based upon adequate consideration which under the law of New York could not be set aside unless unfair or fraudulent.

The decree of divorce determined the taxpayer's obligation to his divorced wife and children, which obligation was subject to modification by the Court as to alimony and custody of the children only. The parties having requested the Court to fix the obligation of the taxpayer to his divorced wife and children, there could be no further or additional obligation on the taxpayer.

The divorce court of the State of New York by Statute is given jurisdiction over questions of alimony and support and custody and maintenance of children. It has no authority to order a defendant husband to set up or establish a trust fund or to transfer the title of any of his property to his wife or his children.

Argument.

Perhaps it should be said at this point that the reason why the taxpayer did not oppose the petition of the Government for the writ of certiorari in this case is that in view of the apparent conflict between the opinion of the Court below and that in other cases in other circuits and particularly because the taxpayer's counsel knew that a writ had been applied for in the case of *Helvering* v. *Fitch*, decided January 29, 1940, No. 243 the taxpayer's counsel was of the opinion that if the writ were granted in the *Fitch* case, it might well be granted in the instant case, the proper decision of which in the opinion of the taxpayer's counsel depends upon a careful analysis of and argument on the facts in the instant case which are peculiarly different from those in any other case cited by the Government or in fact in any other reported case.

The taxpayer Stephen J. Leonard in 1929 was a wealthy individual with an individual estate valued at about two million dollars. His family consisted of his wife and three children two of whom were minors. His wife had on December 27, 1928, instituted in the Supreme Court in New York an action for divorce from him (R. 12). While this action was pending, two agreements were executed both on June 4, 1929, one the aforesaid contract or agreement of trust, the other a separation agreement.

By the terms of Section 1155 of the New York Civil Practice Act, the Court having jurisdiction of an action for divorce instituted by a wife, in the final judgment dissolving the marriage may require the defendant to provide suitably for the education and maintenance of the children of the marriage and for the support of the plaintiff, as justice requires.

having regard to the circumstances of the respective parties; and at any time after final judgment may annul, vary or modify such a direction. Section 1155 refers only to actions instituted for divorce by a wife. By the terms of Section 1170 of the same Act which has to do with an action for divorce or separation brought by either a husband or a wife, it is provided that the court must give such directions as justice requires between the parties for the custody, care, education and maintenance of any of the children of the marriage and where the action is brought by the wife for the support of the wife. Here again also the Court even after final judgment may annul, vary or modify such directions in the interest of justice (Sections 1155 and 1170 are set forth in the Appendix Infra).

In New York as perhaps in many other states of the United States it is customary for counsel to parties engaged in a divorce proceeding as well as the parties themselves to discuss and if possible reduce to writing the agreement of the parties with respect to custody and maintenance of any children of the marriage and provisions for support of the wife. This was done in the instant case and the agreement of the parties set forth in a separation agreement. That agreement gave the sole care and custody of the infant children of the parties to the wife. When the terms of the agreement in respect of the amount of alimony and maintenance were under discussion, a determination thereof naturally included consideration of the financial circumstances of the respective parties. The evidence in this case shows that the taxpayer was at that time a man of wealth. The Board of Tax Appeals has found as a fact that he was worth approximately $2,000,000 (R. 12). The taxpayer's

own uncontradicted testimony (last sentence bottom p. 32 of the Record) is that he decided to divide his fortune, his wife to have one-quarter, his children another quarter and he to retain a half.

In order that the divorce court might have before it the financial circumstances so as to enter a proper decree under the New York Statutes, the separation agreement sets forth and recites those circumstances beginning at Article Third of the agreement (R. 34). There it is recited that the taxpayer has contributed to a trust $650,000 in principal, the net income of which was payable to the wife subject to a prior charge of the first $15,000 of the net income which was payable to the three children of the husband and wife. It is further recited that in addition the wife had received in the past by way of gifts from the husband personal property which at the time of the execution of the separation agreement the parties agreed had a value of at least $350,000 and which the wife agreed had a then present income value of at least $15,000 so that she agreed she had an aggregate income of $30,000 a year. It should be remembered that the husband in addition had given his wife his country home which was worth about $200,000 (R. 32) so that the aggregate of the prior gifts to the wife was thus $550,000. The separation agreement then provided (R. 35) that the husband should pay to his wife "for the support and maintenance of first party (wife) and the aforesaid three children of the parties" $35,000 per year and in addition (R. 36) the husband agreed to pay any extraordinary medical or surgical expenses incurred by the wife or on behalf of the aforesaid three children until the time when each child respectively should attain the age of twenty-five years. Further provision was made that if

after two years from the date of the execution of the separation agreement the ability of the husband to pay the aforesaid $35,000 should be impaired, he could apply to a court for the reduction of that sum to not less than $10,000 per year and conversely if at any time it was so reduced and his financial ability improved, the wife could apply to the Court to increase the payment to an amount never in excess of $35,000 per year.

The specific provision was made in the separation agreement (beginning at the bottom of R. 35) that the husband should not in any way be responsible for any diminution of the net income receivable by the wife from the aforesaid gifts or from the income payable to her by the terms of the trust agreement. The remaining terms of the separation agreement are those customarily found in such documents. The personal property in the former's homes at East Hampton, Long Island and Park Avenue, New York, was confirmed to be that of the wife; the custody of the three children was given to the wife and she released the husband from all claims of dower.

Therefore, on June 4, 1929 when the separation agreement was executed and the separate trust agreement was also executed, the situation of this husband and wife was that they had agreed to continue to live separate and apart; the husband had segregated his fortune so that of the former total family assets of $2,550,000 the wife received confirmation of prior gifts of $550,000, he contributed an additional $650,000 for the children and retained $1,350,000 for himself. He then assumed an obligation to pay from his remaining $1,350,000 or earnings for the support and maintenance of his wife and children $35,000 per year plus any extraordinary medical or surgical expenses of the

wife and children. The arrangements thus made by the parties may be said to be eminently fair. Assuming that the husband might be able to earn upon his retained capital of $1,350,000 a net of 5% or $67,500 per year, the amount thereof ($35,000) which he agreed to pay to his wife for her support and that of the children was somewhat in excess of one-half of what might reasonably be earned. An examination of divorce court decrees in the State of New York would reveal that where the parties to the divorce have children an obligation fixed in the decree for the husband to pay anywhere from a third to a half of his income is reasonable and in fact it is believed that no divorce court would criticize the amount which this husband had obligated himself to pay.

However, at this stage of the proceedings the only obligation which the husband had assumed for the support and maintenance of his wife and children was the aforesaid $35,000 because by the terms of the trust agreement, it did not become irrevocable unless and until a final decree of divorce should be entered (Article 7) (R. 43, 44). Thus had the wife prosecuted the divorce and a decree been entered denying the divorce, the husband would be free to revoke his contribution to the trust but he would still be committed under a valid existing separation agreement to pay his wife $35,000 per year for her support and that of the children.

However, the parties did not rest in that position. The divorce case was prosecuted and a decree of divorce was entered and became final in October, 1929. Shortly thereafter the decree was served on the United States Trust Company of New York as Trustee of the aforesaid trust agreement and by the terms of that agreement it thereupon became irrevocable.

The brief of the Government on this appeal at the top of page 4 states that the divorce court incorporated the agreements (plural) in the decree and approved and affirmed the same. Again at page 6 the brief says that the divorce decree incorporated the agreements (plural) and approved and affirmed them. The evidence in this case refutes such statements. It may be that counsel for the Government meant only by the aforesaid statements in its brief that the reference in the separation agreement to the trust agreement and the incorporation thereof as so recited constitute the ground for the inference in the Government's brief that the divorce court approved the trust agreement. The paragraph in the separation agreement to which the Government may refer is contained in the fourth "Whereas" paragraph of the opening recitation of facts and precedes that part of the separation agreement which sets forth the agreements of the parties thereto. The first two "Whereas" paragraphs set forth jurisdictional facts, namely the date and place of the marriage of the parties and the names and ages of the issue of the marriage; that irreconcilable differences have arisen between the parties and that they are living separate and apart. The third and fourth "Whereas" paragraphs are as follows:

> "WHEREAS, the parties hereto desire to enter into an agreement by the terms of which they may hereafter continue to live separate and apart *and by the terms of which proper and reasonable provision shall be made for the maintenance and support of the party of the first part and the maintenance, support and custody of the aforesaid two daughters and son;* and
>
> "WHEREAS, by *separate* trust agreement bear-

ing even date herewith by and between second party as grantor and United States Trust Company of New York of 25 Wall Street, Borough of Manhattan, City and State of New York, as Trustee, some provision has been made by the second party for the maintenance and support of the first party and the aforesaid two daughters and son, which trust agreement is incorporated herein by reference thereto as though fully and at length set forth and is marked Exhibit A."

It will be noted that in the first of the above quoted paragraphs, it is clearly stated that the parties wish to enter into an agreement by the terms of which proper and reasonable provision shall be made for the maintenance and support of the wife and children. That is not partial provision but entire provision. The sole purpose of the next paragraph is that given to it by Judge Learned Hand in the opinion below, namely, a recitation of the fact that the parties had executed a *separate* trust agreement and that some provision had been made therein for the wife and two daughters and son. Then the separation agreement goes on to state the mutual agreements of the parties which do not in any way conflict with, contain nor incorporate any of the terms of the trust agreement. The real purpose of referring to the trust agreement at all in the separation agreement was to save time and trouble by using the *separation* agreement as a stipulation of facts to be submitted to the court so that it might have before it the financial circumstances of the parties which according to the New York Statute were to be taken into account in fixing the alimony as provided in Section 1155 of the Civil Practice Act of New York. However, an examination of the decree of divorce is sufficient to refute any in-

ference that the court approved the trust agreement. That decree

> "ORDERED, ADJUDGED AND DECREED that the agreement, Exhibit 3, dated June 4, 1929, *providing for the custody of the minor children, Craig Leonard and Stephanie Leonard, issue of said marriage, as well as providing for the support and maintenance of the plaintiff,* be and hereby is approved and affirmed and made a part of the judgment herein, *and as provided in said agreement, Exhibit 3, dated June 4, 1929,* it is
>
> ORDERED, ADJUDGED AND DECREED that the plaintiff herein, Adelaide S. Leonard, have the sole care, custody and control of the infant children, Craig Leonard and Stephanie Leonard, and that the defendant herein, Stephen J. Leonard, pay to the plaintiff herein, Adelaide S. Leonard, for and during the term of her natural life the sum of $35,000 per year."*

The words in italics in the above quotation show that the Court was referring to the separation agreement which provided for the custody of the children and ordered the payment of $35,000 per year alimony "as provided in said agreement, Exhibit 3, dated June 4, 1929" that is, for the support and maintenance of the wife and the children. If the divorce court had intended to approve the trust agreement, it would have so stated in clear terms and referred to the word "trust" in identifying that agreement or otherwise set forth in its order the provisions of the trust agreement. Are we to assume that the divorce court would do a futile thing? Would it attempt to take

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* Note: All italics in this brief have been inserted by the writer unless otherwise noted.

jurisdiction of the trust agreement when the United States Trust Company of New York as Trustee was not before the court? Would it have approved the trust agreement which by its very terms provided that the parties setting up the trust, namely the husband and wife in this case, could change and amend its terms as they alone saw fit? The provisions of the trust in that regard as set forth in Article 12 (R. 49) are as follows:

> "Notwithstanding any of the terms or provisions of Article 7 having to do with the irrevocability of this agreement, this agreement or any of the terms hereof may be changed or amended during the lifetime of the grantor (taxpayer) with the consent of the third party (wife)."

In fact after the divorce both the husband and the wife did amend and change the provisions of the trust agreement. Those changes are set forth in Exhibits 4, 5 and 6 at pages 54 through 73 of the Record. They were introduced in evidence specifically for the purpose of showing that the husband and wife could and did change the arrangements which they had jointly set up without any court, trustee or other approval. There was no reason for the divorce court to approve the trust agreement because the separation agreement specifically provided that the husband "shall in no way be responsible for any diminution of the net income receivable by the first party (wife) by reason of any decrease in income * * * from the trust fund".

Finally, the powers of the divorce court in New York State are entirely statutory. They grant no

power to the court to order a defendant to establish a trust fund or to transfer any of his property to an injured party in a divorce action. The courts in New York have so held. See *Doe* v. *Doe*, 52 Hun 405 (N. Y.) bottom of page 407:

> "The decree seems to make a transfer of the title of the articles so designated to the plaintiff. The ordinary duty of a husband and father is to support his wife and his children, but he is not required to transfer property to them. We think that the law, in cases of separation, intends to compel the husband to do substantially what he was bound to do while his wife and children were living with him, that is, to support them, by supplying their daily needs, not by transferring property to them."

See also *Allen* v. *Farmers' Loan and Trust Co.*, 18 N. Y. App. Div. 27, 35.

It will be remembered that both the husband and the wife executed the contract of trust. Each contributed something as consideration to the other's action. Each desired to protect their children and both desired to reserve control over the children. Neither husband nor wife alone could change the agreement but both together could and thus change the interest of the children therein if they felt such was necessary. The wife gave up her ownership of and right to possibly receive $300,000 when she contributed to the principal of the trust the three policies of insurance on the husband's life which she owned. If the husband died the policies were payable to the trust and thus in effect to the children unless there had been a prior change in the agreement in that regard, because upon the death of the husband no terms of the trust could be changed. *Thus it can not be said that*

this document called a trust agreement was the usual form of trust executed by a husband alone but was a mutual contract providing for the transfer of part of the assets of both the husband and wife to a trust company to be used primarily for the benefit of their children.

The husband contributed to the principal of the trust agreement $400,000 principal amount of McCulloch Oil Company of Delaware 6% bonds; 1100 shares of the capital stock of Bankers Trust Company of New York having a value agreed and fixed by all the parties to the trust agreement of $149,600 and in addition $100,400 in cash or an aggregate of $650,000. It was then provided that on or before January 1, 1930 the husband should withdraw from the trust fund the aforesaid 1100 shares of the capital stock of the Bankers Trust Company and substitute and deposit in place thereof $149,600 in cash and if this were not done that the trustee should sell the shares of Bankers Trust Company stock and deposit the proceeds to the extent of that amount of money in lieu thereof (R. 39). By Article 6 of the trust the husband guaranteed to the trustee (not to the wife) the payment when due of the principal and interest on the $400,000 principal amount of McCulloch Oil Company bonds (R. 43). The purpose of this guarantee is obvious as it was the agreement of both husband and wife that the husband should contribute to the principal of the trust an aggregate of $650,000 in real value because as he had testified, he was setting aside one-quarter of his fortune for his children. As part of the consideration therefore the wife contributed to the principal of the trust the three policies of insurance on the life of the husband in the principal amount of $100,000 each and agreed

to continue to pay the premiums on the policies to the trustee at least three days before the due date for the payment of the premiums (R. 48).

Article 3 of the trust agreement (R. 40) stated that in so far as practicable the net income therefrom should be paid to the life beneficiary or life beneficiaries for the time being entitled thereto in equal monthly instalments. Article 8 of the trust agreement (R. 46) is important to keep in mind. This article provided:

> "From the net income of the trust fund during the life of the third party, the wife of the grantor at the date of the execution of this agreement, the trustee shall pay to each of the following three named children of the third party by the grantor (namely Jeanne Leonard, Stephanie Leonard and Craig Leonard), the sum of Five thousand Dollars ($5,000) per year, except that during the minority of each of said children the $5,000 payable to said minor shall be paid to the third party as natural guardian of and for the account of said minor child; if any of said children shall die during the life of the third party, the $5,000 payable to said child who shall so die shall be thereafter payable to the third party during her life for her own separate use; the remaining net income of the trust fund shall be paid to the third party during her life, to be used by her for her maintenance and support and, in her sole discretion for the support, maintenance, and education of the children, of herself, and the grantor."

ACCORDINGLY, THE FIRST $15,000 IN THE AGGREGATE OF THE NET INCOME FROM THE TRUST OR $5,000 EACH IS PAYABLE AS SHOWN BY THE FOREGOING QUOTATION TO EACH OF THE THREE CHILDREN OF THE TAX-

PAYER WITHOUT ANY LIMITATION OR RESTRICTION AS TO ITS USE FOR THE SUPPORT OR MAINTENANCE OF THE CHILDREN. IF ANY CHILD DIED, THE MOTHER BEING THEN ALIVE, THE $5,000 FORMERLY PAYABLE TO SAID DECEASED CHILD IS THEN PAYABLE TO THE WIFE OF THE TAXPAYER FOR HER OWN SEPARATE USE AND NOT FOR HER MAINTENANCE AND SUPPORT. THEREFORE, NO PART OF THE FIRST $15,000 OF THE INCOME FROM THE TRUST DISCHARGES ANY OBLIGATION OF THE TAXPAYER TO SUPPORT HIS WIFE OR MINOR CHILDREN.

That provision of the trust was necessarily free of any obligation of the husband to support the children because as shown *supra* the separation agreement provided solely for the custody and support of the children and by its terms provided that the $35,000 to be paid by the father should be used for the support and maintenance of the children as well as of the wife. The next sentence of Article 12 provides for the execution of supplemental agreements with the Trustee to provide for any change or amendment and states that immediately upon filing of such supplemental agreement with the Trustee, the amendment shall be deemed effective forthwith. The Article then continues:

> "Nothing in this agreement contained shall be deemed to vest any interest in the children of the third party and the grantor prior to the death of the grantor or the third party, and the said children shall have no right to object to any change or amendment of this agreement which shall be made and or executed with the consent and under the signature of the third party."

Thus it is clear that *both* the husband and the wife could change and either one of them could prevent

any change of any of the terms of the trust agreement. The children had no vested right. The Trustee had no obligation other than to accept the filing of any amendment or change.

The Government in its proposal to tax to the husband the net income of the trust relies upon Sections 22 and 24 of the Revenue Act of 1928 and Article 281 of Regulations 74 promulgated under said Act (Appendix *infra*). That article provides that alimony and an allowance paid under a separation agreement are not deductible from gross income of a taxpayer. The taxpayer has no quarrel with that construction of the Statute and Regulations if it be conceded that the only amount paid or payable by the taxpayer in this case under the separation agreement and divorce decree is the $35,000 provided to be paid in said separation agreement by the husband for the support and maintenance of his wife and children confirmed and approved by the decree of the divorce court.

However, the Government seeks to go further by endeavoring to show that the income from the separate trust set up by the taxpayer and his wife in some way measure the obligation of the husband for the support and maintenance of his wife. This attempt has been rejected by the court below. The attempt of the Government in essence is to say first that the payments to the children, which by the terms of the trust agreement itself were to be payable to the children for their own separate use and not for their maintenance, should be considered as necessarily useable for their maintenance and thus in some way a reduction of the father's paternal liability, and secondly, that so far as payments from the trust fund to the wife are concerned they constitute alimony. It has been shown above that the husband's alimony

was fixed in the decree. It is not believed that this Court would hold that the husband could take the position that his obligation to support his wife and children is measured by the payments from the trust fund and thus if he lost all of his individual property or ability to earn he could require the divorce court in New York to set aside the trust agreement or in any other way reduce or turn back to him the income from the trust or any part thereof. Apparently, the Government in its brief endeavors to sustain an inference set forth in the opinion of the member of the Board of Tax Appeals which was not based on any facts in evidence and which was rejected by the Court below. That inference was that if it had not been for the establishment of the trust, the divorce court would have changed its allowance of alimony and increased it above $35,000. As has been shown *supra* the $35,000 alimony agreed to be paid by the husband in the separation agreement and directed to be paid by the court in its decree was in excess of one-half of the possible income of the husband from his individual estate retained by him after he had made his gifts to his wife and to the children in the trust fund. In the words of Judge Hand of the court below:

> "It seems to us that the intent was that Leonard should never be obliged to make good any deficits caused by decrease in the trust income, or to be relieved by its increase; the original income was taken as the equivalent of a maintenance of $15,000, and discharged him *pro tanto*. That is the more natural view. Possibly, however, there may be an indirect relation between the trust income and the amount fixed in the future by the divorce court under the separation agreement. It is true that the agreement apparently makes the only test the husband's

'circumstances and ability to pay', but that does not necessarily mean that nothing else will be considered. It may be that the wife's other means will also be deemed a factor, and in this way the income of the trust indirectly will determine the allowance. But that circumstance alone is not enough to make that income taxable to him; for if it were, the income from the earlier gifts would be similarly taxable, because that, too, was a factor in the original settlement. Moreover, consistently we should have to go a step further, for it is the commoner practice in fixing alimony to take into consideration the wife's independent income from all sources (citing cases). Obviously it would be absurd to tax the husband upon all this income, and it follows that a more direct correspondence is necessary than anything arising from the power reserved in the decree, even if, as we are disposed not to believe, the income of the trust was not for all purposes to be deemed an equivalent of $15,000."

In the Government's brief beginning at the bottom of page 18 it is stated that the result reached below permits the husband to circumvent an express prohibition in the Statute and Regulations; that is Section 24 and Article 281 of the Regulations. The writer of the Government's brief states:

"Had the grantor held the property without the interposition of the trust, and simply paid out the income therefrom to his wife as alimony he would have been chargeable with the full amount of that income and would not have been entitled to any deduction on account of the alimony paid out. The decision below permits him to achieve the same result by creating a trust but without ren-

dering him liable for tax with respect to the income. In essence, it awards him the very deduction that Congress has denied him."

It is submitted that no such result has been achieved by this taxpayer and that it is not proper to assert that the taxpayer would have been chargeable with the full amount of the trust income. Had the trust been created of the size in this case and the separation agreement merely provided for very small alimony, there might have been some basis for such an inference but as shown above the $35,000 alimony provided for under the separation agreement and divorce decree is more than customarily allowed by divorce courts upon a showing that the divorced husband is worth after a division of this fortune a million and a quarter dollars. In fact if the trust had not been created and the husband taxpayer had retained his fortune of $2,000,000 instead of contributing $650,000 thereof to the trust, it is safe to say that the divorce court upon its own investigation ascertaining the foregoing asset value of the husband, would not have granted alimony in excess of $35,000 per year if it fixed the alimony payable by the husband in accordance with the customary practice in New York. This can be said because taking the husband's assets at $2,000,000 and calculating income thereon at an estimated 5% return, the income would be $100,000 per year and $35,000 alimony would be more than one-third of that income besides which the wife would have had $15,000 income from gifts of over $500,000 previously given her. One is in a very different position if one has set aside out of one's own control $650,000 of one's principal from that if one has that amount in one's own posses-

sion and control to be used in one's business or as one sees fit, the income from which also may be used as one sees fit. The entire $650,000 is then at the risk of the decisions made by oneself and the income can be squandered, imprudently invested or otherwise disposed of at the risk of ordinary commercial business. Once one has divested oneself entirely of the $650,000, has no right to invest it or to otherwise deal with the income, it can no longer be rightly said that the income therefrom is still one's own and in effect a guaranteed income which would never be lost by one if one had it in one's own control. Naught can be said as to what this taxpayer might have done with the $650,000 principal of the trust or the income therefrom had he retained it within his own control. This divorce occurred in 1929, just at the peak of the then stock market orgy. He might have lost the entire principal and income or at least a good part thereof. Had it been used in business it might likewise have disappeared. It is much better surely as a matter of good policy in the protection of a divorced wife and her children to allow the former husband to transfer out of his possession part of his assets if he is willing to do so and cannot be forced to so by court action; to place it in trust with a trust company where it can be invested probably as well as any material investment than to penalize (a) him if he does so by a tax or (b) his wife and children by the risk of possible loss of both principal and income if the husband retains it in his control. Certainly such is true when the husband in contributing to the trust makes no agreement for his own benefit but leaves himself still entirely liable for such orders as to the maintenance and support of his wife and children as the divorce court may decide just.

Much has been said in some of the cases as to a "continuing liability" and in *Helvering* v. *Fitch* (*supra*), this Court held that the income from the trust there involved was taxable to the husband under the general rule enunciated in *Douglas* v. *Willcuts*, 296 U. S. 1, because the taxpayer had failed to show by clear and convincing proof that the Iowa Court had no continuing jurisdiction.

The writer is disposed to agree with the Government's contention that the existence of a continuing power in the divorce court to modify the provision for the wife is not necessarily determinative of the question. As has been referred to, *supra*, under the New York statute a divorce court there retains jurisdiction of parties to a divorce and may amend and modify its final decree.

Without a careful reading of the New York cases which have passed upon the rights of the divorce court to amend and modify payments in divorce cases at the request of petitioners and those New York cases which support the determination that an agreement between parties for the support of the wife can not be modified by a divorce court except where the terms of the agreement are inadequate or unfair might raise some confusion in mind. However, from a careful study it would be realized that the cases divide themselves roughly into the following classes:

(a) Those having to do with contracts made by parties providing for the maintenance and support of a wife and children which are not referred to the divorce court for its consideration and determination, and

(b) Those cases which involve contracts between parties providing for the support and

maintenance of a wife and children which are submitted to the divorce court for its consideration and determination and some of the terms of which become merged in the decree.

Those cases classed in (a) above involve contracts which the courts have held may not be disturbed or set aside unless the terms thereof are inadequate or unfair.

Galusha v. *Galusha*, 116 N. Y. 635, 22 N. E. 1114, 6 L. R. A. 487;
Cain v. *Cain*, 188 App. Div. 780, 177 N. Y. S. 178;
Hamlin v. *Hamlin*, 224 App. Div. 168, 230 N. Y. S. 51.

Those cases classed in (b) involve contracts which the divorce court may subsequently modify or amend *as respects any terms thereof which have to do with the custody of the children and the support of the wife.*

Kunker v. *Kunker*, 230 App. Div. 641, 246 N. Y. S. 118;
Holahan v. *Holahan*, 234 App. Div. 572;
Lowenthal v. *Lowenthal*, 229 App. Div. 446;
Goldfish v. *Goldfish*, 193 App. Div. 686; and
Staehr v. *Staehr*, 260 N. Y. 432.

Accordingly because of the statutory right in New York of the divorce court which is granted complete jurisdiction of all questions having to do with alimony and/or custody and support of children, the divorce court may later change any terms of a contract having to do with alimony and custody and control of children made by a husband and wife which

they have submitted to the divorce court for its approval and which has been ruled upon in the decree. However, it will be observed that even in the latter class of cases referred to under (b) above while a court may modify those terms of a contract which it has approved having to do with custody of children and support of a wife, the court refuses to pass upon any other matters set forth in the contract and relegates the parties to their rights under the contract at law; thus in effect adopting the same attitude as the courts have adopted in the first class of cases that those other provisions of the contract will not be set aside except upon a showing at law of fraud or unfairness. In referring to *Kunker* v. *Kunker, supra*, Judge Learned Hand thought that the case was an exception to the doctrine enumerated in *Galusha* v. *Galusha, Cain* v. *Cain and Hamlin* v. *Hamlin*. It is believed that had Judge Hand noticed the distinction which has been referred to above, he would have understood that *Kunker* v. *Kunker* was not in disagreement with the other cases.

The result of this distinction between the rights of parties under a divorce decree and under their contractual rights, is that in the instant case while the divorce court had the right to change the obligation of the taxpayer and the rights of his wife under the separation agreement as to alimony and custody of the children only, it had no right to change the contract of trust or the other terms and provisions of the separation agreement. That such is the true aspect is shown by the fact that the decree of divorce did not attempt to approve or disapprove or in any way take jurisdiction over the trust agreement. The instant case is one example in the State of New York where a divorce court carefully distinguished its rights under

the Statute to fix the obligations of the husband to his wife and children as to alimony and custody as distinct from any other matters upon which the parties to the contract may have agreed between themselves.

At page 21 of the Government's brief in referring to *Galusha* v. *Galusha, supra,* which held that a fair and binding agreement could not be set aside, the statement is made that that case was decided prior to the enactment of Section 21 of the Domestic Relations Law of 1896 (N. Y. Laws 1896 Vol. 1, c. 272, P. 220) from which was derived Section 51 of the Domestic Relations Law quoted in the appendix. That section empowers a married woman to contract as if unmarried but forbids a husband and wife to contract, alter or dissolve the marriage or to relieve the husband of his liability to support his wife. The Court of Appeals of New York has held that the prohibition just referred to in Section 51 of the Domestic Relations Law does not prevent a husband and wife from entering into a valid separation agreement providing for the maintenance of the wife and the support of children (See *Winter* v. *Winter,* 191 N. Y. 462). While that part of Section 1155 of the New York Civil Practice Act which provides that upon application by either party to a divorce action the court may modify its original decree of divorce was not in the Statute at the time of the decision of *Galusha* v. *Galusha* in 1889 only the first part of the first sentence being then in the Statute, the Statute was amended in 1894 to incorporate the right of modification and subsequent thereto *Cain* v. *Cain* and *Hamlin* v. *Hamlin* were decided reaffirming the fact that a valid agreement between husband and wife not otherwise unfair or overreaching would not be set aside.

At the time of the argument of this case in the court below the writer of this brief stated that in the writer's opinion the decision of this court in *Douglas* v. *Willcuts (supra)*, was based upon the facts that (a) the Minnesota statute authorized the divorce court to order the establishment of a trust fund, something which the New York statute does not permit the divorce court to do; (b) that the decree required the petitioner to provide and create the trust fund; (c) that the petitioner's contention that the District Court did not award alimony was not supported by the terms of the decree as it described the provision in the decree as made "in lieu of all other alimony or interest in the property or estate of the defendant"; and (d) that as such alimony the decree imposed upon the petitioner the obligation to devote the income of the trust through the medium of the trust to the use of the divorced wife.

Judge Learned Hand in his opinion in the court below felt called upon to reverse the lower court's former decision in *Helvering* v. *Brooks* (2 Cir.; 82 F. 2d. 173) and stated that the court below assumed too readily from *Douglas* v. *Willcuts* that any income which in fact relieved the husband from alimony was to be regarded as still his. Judge Hand stated:

> "We failed to consider how carefully the opinion in that case had been based upon the Minnesota law, which continued the husband's duty, and in effect made the trust only a security for whatever the divorce court might from time to time allow. We are satisfied that the Supreme Court did not mean to extend the doctrine to situations where the husband's duty is at an end, and to assess him upon income over which he has no control, and in which he has no interest."

On page 22 of the brief for the Government the statement is made that while under the New York statute the final judgment of divorce ends the relationship of husband and wife, the husband's obligation of support is *continued* in the form of alimony and the court's jurisdiction over the parties and the incidental subject matter does not terminate. It further states that an agreement providing for the wife will be set aside if unfair and unequitable. As has been demonstrated, *supra*, there can be no quarrel with the statement that an agreement providing for the wife will be set aside if unfair and unequitable, but no claim has been made in this case that the trust agreement is at all unfair or unequitable. Hence, it must be sustained. However, it is submitted that the statement in the Government's brief that the husband's obligation of support is *continued* in the form of alimony is not quite correct. As has been well stated by Judge Alton B. Parker in *Galusha* v. *Galusha, supra*, the New York statute authorizes the court in the final judgment dissolving the marriage to require the defendant to provide suitably for the plaintiff as justice requires "because upon the dissolution of the marriage relation the legal obligation of the husband to support the wife ceases". The husband then incurs an entirely new obligation and not a *continuing* obligation, if by the word "continuing" as used in the Government's brief at page 22 is meant an obligation which existed prior to divorce and continues thereafter. Such new obligation arises only from statute, contract or decree of court. The taxpayer in this case contracted by the separation agreement to obligate himself to pay $35,000 a year for the support and maintenance of his wife and children. The court by its decree confirmed such obligation and such obligation only, as

has been well stated by Judge Learned Hand in the opinion below:

> "The question therefore becomes whether this (the fact that there was a settlement agreement as well as a trust agreement) changed the trust into a partial security for a total allowance, made up of the present income of the trust and of so much as the court might from time to time allow, and whether this control over it brings the situation within *Douglas* v. *Willcuts*, *supra*. We think it did not. It seems to us that the intent was that Leonard should never be obliged to make good any deficit caused by decrease in the trust income, or to be relieved by its increase; the original income was taken as the equivalent of a maintenance of $15,000 and discharged him *pro tanto*."

This case involves the taxable year 1929. The Government has made no claim that the divorce decree was in that year or any subsequent year modified in any way as to the obligation of the taxpayer to pay the alimony of $35,000 per year for the support and maintenance of his wife and children as provided in the separation agreement.

CONCLUSION.

The decision of the court below insofar as it held the taxpayer liable to income tax upon the income payable under the terms of the trust agreement to the infant children of the taxpayer should be reversed but in all other respects affirmed.

Respectfully submitted,

J. DONALD DUNCAN,
Attorney for the Respondent.

JAMES B. ALLEY,
JAMES T. BREDIN,
Of Counsel.

APPENDIX.

Revenue Act of 1928, c. 852, 45 Stat. 791:

SEC. 22. GROSS INCOME.

(a) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

* * * * *

SEC. 24. ITEMS NOT DEDUCTIBLE.

(a) *General rule.*—In computing net income no deduction shall in any case be allowed in respect of——

(1) Personal, living, or family expenses;

* * * * *

Treasury Regulations 74, promulgated under the Revenue Act of 1928:

ART. 83. *Gifts and bequests.*—Property received as a gift, or received under a will or under statutes of descent and distribution, is exempt from the income tax, although the income therefrom derived from investment, sale, or otherwise is not. An amount of principal paid under a marriage settlement is a gift. Neither alimony nor an allowance based on a separation agreement is taxable income. (See article 281.)

ART. 281. *Personal and family expenses.*— * * * Alimony and an allowance paid under a separation agreement are not deductible from gross income. (See article 83.) * * *

New York Civil Practice Act, Book 6:

§1155. *Maintenance and support of wife and children in action for divorce by wife.*

The court, in the final judgment dissolving the marriage in an action for divorce brought by the wife, may require the defendant to provide suitably for the education and maintenance of the children of the marriage, and for the support of the plaintiff, as justice requires, having regard to the circumstances of the respective parties; and, by order, upon the application of either party to the action, and after due notice to the other, to be given in such manner as the court shall prescribe, at any time after final judgment whether heretofore or hereafter rendered, may annul, vary or modify such a direction. But no such application shall be made by a defendant unless leave to make the same shall have been previously granted by the court by order made upon or without notice as the court in its discretion may deem proper after presentation to the court of satisfactory proof that justice requires that such an application should be entertained.

§1170. *Custody and maintenance of children, and support of plaintiff in action for divorce or separation.*

Where an action for divorce or separation is brought by either husband or wife, the court, except as otherwise expressly prescribed by statute, must give, either in the final judgment, or by one or more orders, made from time to time

before final judgment, such directions as justice requires, between the parties, for the custody, care, education, and maintenance of any of the children of the marriage, and where the action is brought by the wife, for the support of the plaintiff. The court, by order, upon the application of either party to the action, or any other person or party having the care, custody and control of said child or children pursuant to said final judgment or order, after due notice to the other, to be given in such manner as the court shall prescribe, at any time after final judgment, may annul, vary or modify such directions, or in case no such direction or directions shall have been made, amend it by inserting such direction or directions as justice requires for the custody, care, education and maintenance of any such child or children or for the support of the plaintiff in such final judgment or order or orders. But no such application shall be made by a defendant, or any other person or party having the care, custody and control of said infant or infants, unless leave to make the same shall have been previously granted by the court by order made upon or without notice as the court in its discretion may deem proper after presentation to the court of satisfactory proof that justice requires that such an application should be entertained." (Amended by L. 1921, ch. 199; L. 1925, ch. 240, in effect Sept. 1, 1925.)

The last sentence of Section 1170 was omitted by Laws of 1934, c. 521, in effect September 1.

New York Domestic Relations Law (McKinney's Consolidated Laws of New York, Book 14):

§51. *Powers of married woman.*—A married woman has all the rights in respect to property,

real or personal, and the acquisition, use, enjoyment and disposition thereof, and to make contracts in respect thereto with any person, including her husband, and to carry on any business, trade or occupation, and to exercise all powers and enjoy all rights in respect thereto and in respect to her contracts, and be liable on such contracts, as if she were unmarried; but a husband and wife can not contract to alter or dissolve the marriage or to relieve the husband from his liability to support his wife. * * *

The foregoing provisions of the Civil Practice Act and the Domestic Relations Law were in force in 1929 when the trust and separation agreements in this case were executed and the divorce granted; and, except as above indicated, those provisions have not subsequently been altered or amended.

SUPREME COURT OF THE UNITED STATES.

No. 426.—October Term, 1939.

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner, *vs.* Stephen J. Leonard.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[April 22, 1940.]

Mr. Justice Douglas delivered the opinion of the Court.

This case involves the question of the taxability to the grantor under the Revenue Act of 1928 (45 Stat. 791) of income from a so-called alimony trust which is payable to his divorced wife. We granted certiorari because of the probable conflict of the decision below with *Douglas* v. *Willcuts*, 296 U. S. 1, and *Helvering* v. *Fitch*, 309 U. S. —.

In 1928 respondent's wife instituted suit in New York for an absolute divorce. On June 4, 1929, while that suit was pending, respondent and his wife entered into a separation agreement and, together with a corporate trustee, executed a trust agreement. Under the latter respondent contributed securities and cash of $650,000, which included $400,000 principal amount of 6% first mortgage bonds of an oil company. Respondent guaranteed the "payment when due of the principal and interest" on those bonds; and on notice of any default in the payment of any interest on or principal of them, he agreed to substitute cash or securities with a "market value equal to" the principal, and cash sufficient to cover any accrued interest.[1] The trust was irrevocable[2] except that (1) it could be amended by respondent and his wife;[3] and (2) respondent retained a limited power of substitution as respects certain

[1] No extension of the time of payment of principal or interest on these bonds was to be made without the consent of the wife and without the extension of the guarantee of respondent or his personal representative.

[2] Except on discontinuance or dismissal of the divorce action.

[3] It was so amended three times but in respects not material here.

bank stock which was part of the corpus. The trustee agreed to use "reasonable efforts to consult" with respondent with respect to "the character of the investments" though it was not bound to follow his advice. Respondent retained no right to either the corpus or the income, or any part thereof, except as indicated above. The net income was to be paid as follows: $5000 a year to each of three children; the remaining amount to the wife during her life for her maintenance and support, and in her sole discretion for the support, maintenance and education of the children. On death of the wife, the corpus was to be held for the children.

The separation agreement incorporated the trust agreement by reference; stated that the wife's income from the trust and from other property received from the husband would aggregate $30,000 a year; provided that respondent would pay his wife an additional $35,000 each year during her life so that her aggregate net income for the maintenance and support of herself and the children would approximate $65,000 a year, and would further pay any "extraordinary medical or surgical expenses" incurred by the wife or on behalf of the children until they attained the age of twenty-five years; stated that in the event that respondent's ability to pay the above $35,000 became impaired, he might apply to any court of competent jurisdiction for a reduction of his obligation to not less than $10,000 a year; made other property settlements; provided for care and custody of the children; released dower, etc.

The decree of divorce became final in October 1929. It "approved and affirmed and made a part of the judgment herein" the separation agreement (which as we have said incorporated the trust agreement) "providing for the support and maintenance of the plaintiff", and in addition directed respondent to pay her $35,000 a year for the rest of her life. From June 4, 1929 to December 31, 1929, the trustee received $16,191.34 as dividends and interest from the trust property. It distributed $5200 to the wife and $2083.33 to each of the three children, leaving an undistributed balance for that period of about $4700. Respondent did not include any of that income in his return for 1929. The Commissioner determined a deficiency. The Board of Tax Appeals held that only the amounts actually distributed to respondent's wife and minor children were taxable to him. 36 B. T. A. 563. The

Circuit Court of Appeals reversed, holding that respondent, though taxable on income payable to his minor children, was not taxable on income payable to the wife. 105 F. (2d) 900.

Here, as in the Circuit Court of Appeals, it was urged by the petitioner that this alimony trust was merely security for respondent's continuing obligation to support his wife and, therefore, that the trust income payable to her was taxable to him under the rule of *Douglas* v. *Willcuts, supra.* In support of that position it was urged, *inter alia*, that under New York law respondent's obligation was not discharged since the New York court retained the power to modify the decree; and that the promise by respondent to pay the wife $35,000 (or in no event less than $10,000) a year converted the trust into at least partial security for the total allowance to her. In either of such events the rule of *Douglas* v. *Willcuts, supra,* would apply. See *Helvering* v. *Fitch, supra.* The Circuit Court of Appeals, however, decided these two questions adversely to petitioner. But there is one matter not touched on by that court which we think is determinative of one phase of the case.

The trust agreement contains an express personal obligation of respondent in the form of a guarantee of payment of the principal and interest on $400,000 of the 6% bonds which were part of the trust corpus. To be sure, that personal obligation was contingent. But we do not deem that to be material. We recently stated in *Helvering* v. *Fitch, supra*, p. —, that under this statutory scheme escape from the rule of *Douglas* v. *Willcuts, supra*, may be had only on "clear and convincing proof" that "local law and the alimony trust have given the divorced husband a full discharge and leave no continuing obligation however contingent." Whatever may be the correct view on the other aspects of the case, the guarantee was such a continuing obligation. The fact that the wife or other beneficiaries looked primarily to the trust and only secondarily to respondent for payment of $24,000 annually, the fact that respondent's obligation might be enforceable by the trustee, the fact that respondent might never have to make good on his promise are beside the point. The existence of wholly contingent obligations, whether contractual or otherwise, is adequate to support the results reached in *Douglas* v. *Willcuts, supra.* For in that case it was manifest that at the time of the creation and approval of the trust the divorce court might never exercise its reserved power to revise

or alter the decree and the husband might never have to make good on his promise to make up deficiencies in the estimated trust income. Likewise in the instant case, it cannot be said that the divorce decree and the alimony trust gave respondent an absolute discharge from his prior obligation. So far as the guarantee alone is concerned, they permitted his preexisting unconditional duty to be transformed into a limited contingent one. But nonetheless they placed a specific and adequate sanction on that duty, so that respondent's personal obligation would not be fully discharged at least until complete payment of the principal and interest on the 6% bonds had been made. Thus in effect, if not in form, the trust agreement was security for his continuing obligation which would be discharged at least *pro tanto* as income from those bonds was received by the trustee. Hence the case in substance is the same as those where pursuant to contract or arrangement an obligation is discharged by another for the taxpayer's benefit; see *Old Colony Trust Co.* v. *Commissioner*, 279 U. S. 716; *United States* v. *Boston & Maine Railroad*, 279 U. S. 732; or where the taxpayer creates a trust, the income of which is applied to the discharge of his debt. See *Helvering* v. *Blumenthal*, 296 U. S. 552. Here, as there, the taxpayer received a benefit by the payments. The catalogue of benefits is not depleted when primary obligations are discharged. For these reasons that portion of the trust income which was received from the guaranteed bonds was clearly taxable to respondent.

Apparently, however, a portion of that income was received from other trust property. But we think that was also taxable to respondent though for another reason.

As we have seen the divorce decree approved, affirmed and made part of the judgment the separation agreement providing for the "support and maintenance" of the wife. Her maintenance and support were secured not only by the trust agreement and other property settlements but also by the personal obligation of the husband to contribute an annual sum. The Circuit Court of Appeals held that under New York law the terms of the trust would not be changed "unless the wife can disaffirm it for fraud, overreaching, or the like", citing *Galusha* v. *Galusha*, 116 N. Y. 635, 138 N. Y. 272; *Cain* v. *Cain*, 188 A. D. 780; *Hamlin* v. *Hamlin*, 224 A. D. 168. If the case was here on application of local law under the rule

of *Erie Railroad Co.* v. *Tompkins*, 304 U. S. 64, we would not be inclined to disturb that finding. But it is not. Here respondent is seeking to escape one of the normal incidents of the federal income tax. For that purpose he invokes the aid of New York law. In *Helvering* v. *Fitch*, *supra*, we stated that where the divorced husband desires to avoid the general rule expressed in *Douglas* v. *Willcuts*, *supra*, he carries a distinct burden of establishing not by mere inference and conjecture but by "clear and convincing proof" that local law and the alimony trust have given him a full discharge. We do not think that respondent has sustained that burden.

As stated by the Circuit Court of Appeals, it does seem clear that mere property settlements, though incorporated into the decree, may not be modified pursuant to the reserved statutory powers of the court, contained in N. Y. Civil Prac. Act §§ 1155, 1170. See *Cain* v. *Cain*, *supra*; *Goldfish* v. *Goldfish*, 193 A. D. 686; *Schnitzer* v. *Buerger*, 237 A. D. 622. Nevertheless these settlements may be remade by the court not only where an ordinary contract may be set aside but also where they are unfair, inequitable and unjust. *Hamlin* v. *Hamlin*, *supra*. Cf. *Tirrell* v. *Tirrell*, 232 N. Y. 224. As stated by the court in the *Hamlin* case (224 A. D. at p. 171) the requirement is that "such contracts be not only free from taint of actual fraud or coercion but also fair and reasonably sufficient having regard to the station in life and circumstances of the parties." More important to this case, however, are *Kunker* v. *Kunker*, 230 A. D. 641 and *Holahan* v. *Holahan*, 234 A. D. 572. They make it plain that the covenants of a separation agreement are not "an insuperable obstacle to obtaining relief by modification of the allowances." *Holahan* v. *Holahan*, *supra*, p. 574. Cf. *Severance* v. *Severance*, 260 N. Y. 432. The reserved power apparently may be exercised where the provision in the separate agreement, approved by the decree, is for support and maintenance (*Kunker* v. *Kunker* and *Holahan* v. *Holahan*, *supra*) but not where it is in settlement of claims of ownership to specified property. *Goldfish* v. *Goldfish* and *Schnitzer* v. *Buerger*, *supra*. The provisions of the separation agreement and the trust agreement here in question specifically relate to and were designed to afford support and maintenance for the wife. Unlike the purpose of the trust agreement in *Schnitzer* v. *Buerger*, *supra*, the purpose here apparently was not to compose any controversies over the securities. We need not decide whether the court retained the

power to require respondent to make additional payments to the wife in case, say, all the securities in trust turned out to be worthless. All we do hold is that respondent has not shown by "clear and convincing proof" that the court lacks the power to add to his personal obligations in any such circumstances.

Reversed.

Mr. Justice REED concurs in the result for the reasons stated in the dissent in *Helvering* v. *Fuller*, decided today, No. 427 October Term, 1939.

The CHIEF Justice, Mr. Justice MCREYNOLDS, and Mr. Justice ROBERTS are of the opinion that the judgment of the Circuit Court of Appeals should be affirmed.

A true copy.

Test:

Clerk, Supreme Court, U. S.